

NATIONAL FUEL GAS CO

Form 10-K

November 26, 2008

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**UNITED STATES SECURITIES AND EXCHANGE COMMISSION
Washington, D.C. 20549
Form 10-K**

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

For the Fiscal Year Ended September 30, 2008

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

For the Transition Period from to

Commission File Number 1-3880

National Fuel Gas Company

(Exact name of registrant as specified in its charter)

New Jersey

*(State or other jurisdiction of
incorporation or organization)*

6363 Main Street

Williamsville, New York

(Address of principal executive offices)

13-1086010

*(I.R.S. Employer
Identification No.)*

14221

(Zip Code)

(716) 857-7000

Registrant's telephone number, including area code

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

Title of Each Class	Name of Each Exchange on Which Registered
Common Stock, \$1 Par Value, and Common Stock Purchase Rights	New York Stock Exchange

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 No

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

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

Indicate by check mark 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 the 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.

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. (Check one):

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

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

The aggregate market value of the voting stock held by nonaffiliates of the registrant amounted to \$3,768,755,000 as of March 31, 2008.

Common Stock, \$1 Par Value, outstanding as of October 31, 2008: 79,124,644 shares.

DOCUMENTS INCORPORATED BY REFERENCE

Portions of the registrant's definitive Proxy Statement for its 2009 Annual Meeting of Stockholders are incorporated by reference into Part III of this report.

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Glossary of Terms

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

National Fuel Gas Companies

Company The Registrant, the Registrant and its subsidiaries or the Registrant's subsidiaries as appropriate in the context of the disclosure

Data-Track Data-Track Account Services, Inc.

Distribution Corporation National Fuel Gas Distribution Corporation

Empire Empire State Pipeline

ESNE Energy Systems North East, LLC

Highland Highland Forest Resources, Inc.

Horizon Horizon Energy Development, Inc.

Horizon B.V. Horizon Energy Development B.V.

Horizon LFG Horizon LFG, Inc.

Horizon Power Horizon Power, Inc.

Leidy Hub Leidy Hub, Inc.

Midstream National Fuel Gas Midstream Corporation

Model City Model City Energy, LLC

National Fuel National Fuel Gas Company

NFR National Fuel Resources, Inc.

Registrant National Fuel Gas Company

SECI Seneca Energy Canada Inc.

Seneca Seneca Resources Corporation

Seneca Energy Seneca Energy II, LLC

Supply Corporation National Fuel Gas Supply Corporation

Toro Toro Partners, LP

U.E. United Energy, a.s.

Regulatory Agencies

EPA United States Environmental Protection Agency

FASB Financial Accounting Standards Board

FERC Federal Energy Regulatory Commission

NYDEC New York State Department of Environmental Conservation

NYPSC State of New York Public Service Commission

PaPUC Pennsylvania Public Utility Commission

SEC Securities and Exchange Commission

Other

APB 18 Accounting Principles Board Opinion No. 18, The Equity Method of Accounting for Investments in Common Stock

APB 25 Accounting Principles Board Opinion No. 25, Accounting for Stock Issued to Employees

ARB 51 Accounting Research Bulletin No. 51, Consolidated Financial Statements

Bbl Barrel (of oil)

Bcf Billion cubic feet (of natural gas)

Bcfe (or Mcfe) represents Bcf (or Mcf) Equivalent The total heat value (Btu) of natural gas and oil expressed as a volume of natural gas. National Fuel uses a conversion formula of 1 barrel of oil = 6 Mcf of natural gas.

Board foot A measure of lumber and/or timber equal to 12 inches in length by 12 inches in width by one inch in thickness.

Btu British thermal unit; the amount of heat needed to raise the temperature of one pound of water one degree Fahrenheit.

Capital expenditure Represents additions to property, plant, and equipment, or the amount of money a company spends to buy capital assets or upgrade its existing capital assets.

Degree day A measure of the coldness of the weather experienced, based on the extent to which the daily average temperature falls below a reference temperature, usually 65 degrees Fahrenheit.

Derivative A financial instrument or other contract, the terms of which include an underlying variable (a price, interest rate, index rate, exchange rate, or other variable) and a notional amount (number of units, barrels, cubic feet, etc.). The terms also permit for the instrument or contract to be settled net, and no initial net investment is required to enter into the financial instrument or contract. Examples include futures contracts, options, no cost collars and swaps.

Development costs Costs incurred to obtain access to proved reserves and to provide facilities for extracting, treating, gathering and storing the oil and gas.

Development well A well drilled to a known producing formation in a previously discovered field.

Dth Decatherm; one Dth of natural gas has a heating value of 1,000,000 British thermal units, approximately equal to the heating value of 1 Mcf of natural gas.

Exchange Act Securities Exchange Act of 1934, as amended

Expenditures for long-lived assets Includes capital expenditures, stock acquisitions and/or investments in partnerships.

Exploitation Development of a field, including the location, drilling, completion and equipment of wells necessary to produce the commercially recoverable oil and gas in the field.

Exploration costs Costs incurred in identifying areas that may warrant examination, as well as costs incurred in examining specific areas, including drilling exploratory wells.

Exploratory well A well drilled in unproven or semi-proven territory for the purpose of ascertaining the presence underground of a commercial hydrocarbon deposit.

FIN FASB Interpretation Number

FIN 47 FASB Interpretation No. 47, Accounting for Conditional Asset Retirement Obligations an Interpretation of SFAS 143.

FIN 48 FASB Interpretation No. 48, Accounting for Uncertainty in Income Taxes an Interpretation of SFAS 109.

Firm transportation and/or storage The transportation and/or storage service that a supplier of such service is obligated by contract to provide and for which the customer is obligated to pay whether or not the service is utilized.

GAAP Accounting principles generally accepted in the United States of America

Goodwill An intangible asset representing the difference between the fair value of a company and the price at which a company is purchased.

Grid The layout of the electrical transmission system or a synchronized transmission network.

Hedging A method of minimizing the impact of price, interest rate, and/or foreign currency exchange rate changes, often times through the use of derivative financial instruments.

Hub Location where pipelines intersect enabling the trading, transportation, storage, exchange, lending and borrowing of natural gas.

Interruptible transportation and/or storage The transportation and/or storage service that, in accordance with contractual arrangements, can be interrupted by the supplier of such service, and for which the customer does not pay unless utilized.

LIBOR London Interbank Offered Rate

LIFO Last-in, first-out

Mbbl Thousand barrels (of oil)

Mcf Thousand cubic feet (of natural gas)

MD&A Management's Discussion and Analysis of Financial Condition and Results of Operations

MDth Thousand decatherms (of natural gas)

MMcf Million cubic feet (of natural gas)

MMcfe Million cubic feet equivalent

NYMEX New York Mercantile Exchange. An exchange which maintains a futures market for crude oil and natural gas.

Open Season A bidding procedure used by pipelines to allocate firm transportation or storage capacity among prospective shippers, in which all bids submitted during a defined time period are evaluated as if they had been submitted simultaneously.

Order 636 An order issued by FERC entitled "Pipeline Service Obligations and Revisions to Regulations Governing Self-Implementing Transportation Under Part 284 of the Commission's Regulations."

PCB Polychlorinated Biphenyl

Proved developed reserves Reserves that can be expected to be recovered through existing wells with existing equipment and operating methods.

Proved undeveloped reserves Reserves that are expected to be recovered from new wells on undrilled acreage, or from existing wells where a relatively major expenditure is required to make these reserves productive.

PRP Potentially responsible party

PUHCA 1935 Public Utility Holding Company Act of 1935

PUHCA 2005 Public Utility Holding Company Act of 2005

Reserves The unproduced but recoverable oil and/or gas in place in a formation which has been proven by production.

Restructuring Generally referring to partial deregulation of the utility industry by statutory or regulatory process. Restructuring of federally regulated natural gas pipelines resulted in the separation (or unbundled) of gas commodity service from transportation service for wholesale and large-volume retail markets. State restructuring programs attempt to extend the same process to retail mass markets.

SAR Stock-settled stock appreciation right

SFAS Statement of Financial Accounting Standards

SFAS 5 Statement of Financial Accounting Standards No. 5, Accounting for Contingencies

SFAS 69 Statement of Financial Accounting Standards No. 69, Disclosures about Oil and Gas Producing Activities

SFAS 71 Statement of Financial Accounting Standards No. 71, Accounting for the Effects of Certain Types of Regulation

SFAS 87 Statement of Financial Accounting Standards No. 87, Employers Accounting for Pensions

SFAS 88 Statement of Financial Accounting Standards No. 88, Employers Accounting for Settlements and Curtailments of Defined Benefit Pension Plans and for Termination Benefits

SFAS 106 Statement of Financial Accounting Standards No. 106, Employers Accounting for Postretirement Benefits Other Than Pensions.

SFAS 109 Statement of Financial Accounting Standards No. 109, Accounting for Income Taxes

SFAS 112 Statement of Financial Accounting Standards No. 112, Employers Accounting for Postemployment Benefits, an amendment of SFAS 5 and 43

SFAS 115 Statement of Financial Accounting Standards No. 115, Accounting for Certain Investments in Debt and Equity Securities

SFAS 123 Statement of Financial Accounting Standards No. 123, Accounting for Stock-Based Compensation

SFAS 123R Statement of Financial Accounting Standards No. 123R, Share-Based Payment

SFAS 132R Statement of Financial Accounting Standards No. 132R, Employers Disclosures about Pensions and Other Postretirement Benefits

SFAS 133 Statement of Financial Accounting Standards No. 133, Accounting for Derivative Instruments and Hedging Activities

SFAS 141R Statement of Financial Accounting Standards No. 141R, Business Combinations

SFAS 142 Statement of Financial Accounting Standards No. 142, Goodwill and Other Intangible Assets

SFAS 143 Statement of Financial Accounting Standards No. 143, Accounting for Asset Retirement Obligations

SFAS 157 Statement of Financial Accounting Standards No. 157, Fair Value Measurements

SFAS 158 Statement of Financial Accounting Standards No. 158, Employers Accounting for Defined Benefit Pension and Other Postretirement Plans, an Amendment of SFAS 87, 88, 106, and 132R

SFAS 159 Statement of Financial Accounting Standards No. 159, The Fair Value Option for Financial Assets and Financial Liabilities Including an Amendment of SFAS 115

SFAS 160 Statement of Financial Accounting Standards No. 160, Noncontrolling Interests in Consolidated Financial Statements, an Amendment of ARB 51

SFAS 161 Statement of Financial Accounting Standards No. 161, Disclosures about Derivative Instruments and Hedging Activities, an Amendment of SFAS 133

Spot gas purchases The purchase of natural gas on a short-term basis.

Stock acquisitions Investments in corporations.

Unbundled service A service that has been separated from other services, with rates charged that reflect only the cost of the separated service.

VEBA Voluntary Employees Beneficiary Association

WNC Weather normalization clause; a clause in utility rates which adjusts customer rates to allow a utility to recover its normal operating costs calculated at normal temperatures. If temperatures during the measured period are warmer than normal, customer rates are adjusted upward in order to recover projected operating costs. If temperatures during the measured period are colder than normal, customer rates are adjusted downward so that only the projected operating costs will be recovered.

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This Form 10-K contains forward-looking statements as defined by the Private Securities Litigation Reform Act of 1995. Forward-looking statements should be read with the cautionary statements included in this Form 10-K at Item 7, MD&A, under the heading Safe Harbor for Forward-Looking Statements. Forward-looking statements are all statements other than statements of historical fact, including, without limitation, statements regarding future prospects, plans, objectives, goals, projections, strategies, future events or performance and underlying assumptions, capital structure, anticipated capital expenditures, completion of construction and other projects, projections for pension and other post-retirement benefit obligations, impacts of the adoption of new accounting rules, and possible outcomes of litigation or regulatory proceedings, as well as statements that are identified by the use of the words anticipates, estimates, expects, forecasts, intends, plans, predicts, projects, believes, seeks, will, and may a

PART I

Item 1 Business

The Company and its Subsidiaries

National Fuel Gas Company (the Registrant), incorporated in 1902, is a holding company organized under the laws of the State of New Jersey. Except as otherwise indicated below, the Registrant owns directly or indirectly all of the outstanding securities of its subsidiaries. Reference to the Company in this report means the Registrant, the Registrant and its subsidiaries or the Registrant's subsidiaries as appropriate in the context of the disclosure. Also, all references to a certain year in this report relate to the Company's fiscal year ended September 30 of that year unless otherwise noted.

The Company is a diversified energy company and reports financial results for five business segments.

1. The Utility segment operations are carried out by National Fuel Gas Distribution Corporation (Distribution Corporation), a New York corporation. Distribution Corporation sells natural gas or provides natural gas transportation services to approximately 727,000 customers through a local distribution system located in western New York and northwestern Pennsylvania. The principal metropolitan areas served by Distribution Corporation include Buffalo, Niagara Falls and Jamestown, New York and Erie and Sharon, Pennsylvania.

2. The Pipeline and Storage segment operations are carried out by National Fuel Gas Supply Corporation (Supply Corporation), a Pennsylvania corporation, and Empire State Pipeline (Empire), a New York joint venture between two wholly owned subsidiaries of the Company. Supply Corporation provides interstate natural gas transportation and storage services for affiliated and nonaffiliated companies through (i) an integrated gas pipeline system extending from southwestern Pennsylvania to the New York-Canadian border at the Niagara River and eastward to Ellisburg and Leidy, Pennsylvania, and (ii) 27 underground natural gas storage fields owned and operated by Supply Corporation as well as four other underground natural gas storage fields owned and operated jointly with other interstate gas pipeline companies. Empire, an intrastate pipeline company acquired by the Company in 2003, transports natural gas for Distribution Corporation and for other utilities, large industrial customers and power producers in New York State. Empire owns the Empire Pipeline, which is a 157-mile pipeline that extends from the United States/Canadian border at the Niagara River near Buffalo, New York to near Syracuse, New York. Empire is constructing the Empire Connector project, which consists of a compressor station and a 77-mile pipeline extension from near Rochester, New York to an interconnection near Corning, New York with the unaffiliated Millennium Pipeline project, which is also under construction. The Millennium Pipeline is expected to serve the New York City area upon its completion. Upon completion of the Empire Connector and Millennium Pipeline projects, which is currently expected to occur in December 2008, the Company expects that Empire will become an interstate pipeline company and will merge into Empire Pipeline, Inc. as described below.

3. The Exploration and Production segment operations are carried out by Seneca Resources Corporation (Seneca), a Pennsylvania corporation. Seneca is engaged in the exploration for, and the development and purchase of, natural gas and oil reserves in California, in the Appalachian region of the United States, in Wyoming, and in the Gulf Coast region of Texas, Louisiana, and Alabama, including offshore areas in federal

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waters and some state waters. At September 30, 2008, the Company had U.S. reserves of 46,198 Mbbl of oil and 225,899 MMcf of natural gas.

In 2007, Seneca sold its subsidiary, Seneca Energy Canada Inc. (SECI), which conducted exploration and production operations in the provinces of Alberta, Saskatchewan and British Columbia in Canada.

4. The Energy Marketing segment operations are carried out by National Fuel Resources, Inc. (NFR), a New York corporation, which markets natural gas to industrial, wholesale, commercial, public authority and residential customers primarily in western and central New York and northwestern Pennsylvania, offering competitively priced natural gas for its customers.

5. The Timber segment operations are carried out by Highland Forest Resources, Inc. (Highland), a New York corporation, and by a division of Seneca known as its Northeast Division. This segment markets timber from its New York and Pennsylvania land holdings, owns two sawmill operations in northwestern Pennsylvania and processes timber consisting primarily of high quality hardwoods. At September 30, 2008, the Company owned 103,680 acres of timber property and managed an additional 3,122 acres of timber rights.

Financial information about each of the Company's business segments can be found in Item 7, MD&A and also in Item 8 at Note J Business Segment Information.

The Company's other direct wholly owned subsidiaries are not included in any of the five reported business segments and consist of the following:

Horizon Energy Development, Inc. (Horizon), a New York corporation formed to engage in foreign and domestic energy projects through investments as a sole or substantial owner in various business entities. These entities include Horizon's wholly owned subsidiary, Horizon Energy Holdings, Inc., a New York corporation, which owns 100% of Horizon Energy Development B.V. (Horizon B.V.). Horizon B.V. is a Dutch company that is in the process of winding up or selling certain power development projects in Europe;

Horizon LFG, Inc. (Horizon LFG), a New York corporation engaged through subsidiaries in the purchase, sale and transportation of landfill gas in Ohio, Michigan, Kentucky, Missouri, Maryland and Indiana. Horizon LFG and one of its wholly owned subsidiaries own all of the partnership interests in Toro Partners, LP (Toro), a limited partnership which owns and operates short-distance landfill gas pipeline companies. The Company acquired Toro in June 2003;

Leidy Hub, Inc. (Leidy Hub), a New York corporation formed to provide various natural gas hub services to customers in the eastern United States;

Data-Track Account Services, Inc. (Data-Track), a New York corporation formed to provide collection services principally for the Company's subsidiaries;

Horizon Power, Inc. (Horizon Power), a New York corporation which is an exempt wholesale generator under PUHCA 2005 and is developing or operating mid-range independent power production facilities and landfill gas electric generation facilities;

Empire Pipeline, Inc., a New York corporation formed in 2005 to be the surviving corporation of a planned future merger with Empire, which is expected to occur after construction of the Empire Connector project (described below under the heading Rates and Regulation and under Item 7, MD&A under the headings Investing Cash Flow and Rate and Regulatory Matters); and

National Fuel Gas Midstream Corporation, a Pennsylvania corporation formed to build, own and operate natural gas processing and pipeline gathering facilities in the Appalachian region.

No single customer, or group of customers under common control, accounted for more than 10% of the Company's consolidated revenues in 2008.

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Rates and Regulation

The Registrant is a holding company as defined under PUHCA 2005. PUHCA 2005 repealed PUHCA 1935, to which the Company was formerly subject, and granted the FERC and state public utility commissions access to certain books and records of companies in holding company systems. Pursuant to the FERC's regulations under PUHCA 2005, the Company and its subsidiaries are exempt from the FERC's books and records regulations under PUHCA 2005.

The Utility segment's rates, services and other matters are regulated by the NYPSC with respect to services provided within New York and by the PaPUC with respect to services provided within Pennsylvania. For additional discussion of the Utility segment's rates and regulation, see Item 7, MD&A under the heading "Rate and Regulatory Matters" and Item 8 at Note C "Regulatory Matters."

The Pipeline and Storage segment's rates, services and other matters are currently regulated by the FERC with respect to Supply Corporation and by the NYPSC with respect to Empire. The FERC has authorized Empire to construct and operate additional facilities (the Empire Connector project) and to become a FERC-regulated interstate pipeline company upon placement of those facilities into service, which is currently expected to occur in December 2008. For additional discussion of the Pipeline and Storage segment's rates and regulation, see Item 7, MD&A under the heading "Rate and Regulatory Matters" and Item 8 at Note C "Regulatory Matters." For further discussion of the Empire Connector project, refer to Item 7, MD&A under the headings "Investing Cash Flow" and "Rate and Regulatory Matters."

The discussion under Item 8 at Note C "Regulatory Matters" includes a description of the regulatory assets and liabilities reflected on the Company's Consolidated Balance Sheets in accordance with applicable accounting standards. To the extent that the criteria set forth in such accounting standards are not met by the operations of the Utility segment or the Pipeline and Storage segment, as the case may be, the related regulatory assets and liabilities would be eliminated from the Company's Consolidated Balance Sheets and such accounting treatment would be discontinued.

In addition, the Company and its subsidiaries are subject to the same federal, state and local (including foreign) regulations on various subjects, including environmental matters, to which other companies doing similar business in the same locations are subject.

The Utility Segment

The Utility segment contributed approximately 22.9% of the Company's 2008 net income available for common stock.

Additional discussion of the Utility segment appears below in this Item 1 under the headings "Sources and Availability of Raw Materials," "Competition: The Utility Segment" and "Seasonality," in Item 7, MD&A and in Item 8, Financial Statements and Supplementary Data.

The Pipeline and Storage Segment

The Pipeline and Storage segment contributed approximately 20.1% of the Company's 2008 net income available for common stock.

Supply Corporation has service agreements for all of its firm storage capacity, totaling 68,408 MDth. The Utility segment has contracted for 27,865 MDth or 40.7% of the total firm storage capacity, and the Energy Marketing segment accounts for another 4,811 MDth or 7.1% of the total firm storage capacity. Nonaffiliated customers have

contracted for the remaining 35,732 MDth or 52.2% of the total firm storage capacity. The majority of Supply Corporation's storage and transportation services are performed under contracts that allow Supply Corporation or the shipper to terminate the contract upon six or twelve months' notice effective at the end of the contract term. The contracts also typically include "evergreen" language designed to allow the contracts to extend year-to-year at the end of the primary term. At the beginning of 2009, 72.0% of Supply Corporation's total firm storage capacity was committed under contracts that, subject to 2008 shipper or Supply Corporation notifications, could have been terminated effective in 2009. Supply Corporation did not issue or

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receive any such storage contract termination notifications in 2008. The strong demand for market-area storage enabled Supply Corporation to eliminate its remaining storage service rate discounts in 2007, and effective April 1, 2008, all storage services were contracted at the maximum tariff rates.

Supply Corporation's firm transportation capacity is not limited to a fixed quantity, due to the diverse weblike nature of its pipeline system, and is subject to change as the market identifies different transportation paths and receipt/delivery point combinations. Supply Corporation currently has firm transportation service agreements for approximately 2,117 MDth per day (contracted transportation capacity). The Utility segment accounts for approximately 1,065 MDth per day or 50.3% of contracted transportation capacity, and the Energy Marketing and Exploration and Production segments represent another 102 MDth per day or 4.8% of contracted transportation capacity. The remaining 950 MDth or 44.9% of contracted transportation capacity is subject to firm contracts with nonaffiliated customers.

At the beginning of 2009, 49.3% of Supply Corporation's contracted transportation capacity was committed under affiliate contracts that were scheduled to expire in 2009 or, subject to 2008 shipper or Supply Corporation notifications, could have been terminated effective in 2009. Based on contract expirations and termination notices received in 2008 for 2009 termination, and taking into account any known contract additions, contracted transportation capacity with affiliates is expected to decrease 0.3% in 2009. Similarly, 26.7% of contracted transportation capacity was committed under unaffiliated shipper contracts that were scheduled to expire in 2009 or, subject to 2008 shipper or Supply Corporation notifications, could have been terminated effective in 2009. Based on contract expirations and termination notices received in 2008 for 2009 termination, and taking into account any known contract additions, contracted transportation capacity with unaffiliated shippers is expected to increase 9.4% in 2009. This increase is due largely to the addition of compression at various facilities throughout the system as well as other projects designed to create incremental transportation capacity. Supply Corporation previously has been successful in marketing and obtaining executed contracts for available transportation capacity (at discounted rates when necessary), and expects this success to continue.

For the 2008-2009 winter period, Empire has service agreements in place for the full amount of its firm transportation capacity to its existing delivery points, totaling approximately 547 MDth per day. Most of Empire's firm capacity (91.2%) has been contracted as long-term full-year deals. A small number of those contracts are due to expire during fiscal 2009, representing 1.4% of Empire's firm capacity. In addition, Empire has some seasonal (winter-only) contracts that extend for multiple years, representing 2.7% of Empire's firm capacity. One of those seasonal contracts is due to expire during fiscal 2009; representing 1.1% of Empire's firm capacity. Arrangements for the remaining 6.1% of Empire's firm capacity are seasonal or annual contracts that expire before the end of fiscal 2009. Empire expects that all available capacity arising from expiring agreements will be re-contracted under new seasonal or annual agreements. The Utility segment accounts for approximately 7.8% of Empire's firm capacity, and the Energy Marketing segment accounts for approximately 1.9% of Empire's firm capacity, with the remaining 90.3% of Empire's firm capacity subject to contracts with nonaffiliated customers.

Upon the completion of the Empire Connector project, Empire will have expansion capacity for the 2008-2009 winter period. Empire has a firm service agreement for 150.7 MDth per day of this expansion capacity. This long-term full-year agreement represents approximately 60% of the Empire Connector expansion capacity. The Company continues to market the remaining capacity on both a firm and interruptible basis. None of this contracted expansion capacity will expire during fiscal 2009.

Additional discussion of the Pipeline and Storage segment appears below under the headings Sources and Availability of Raw Materials, Competition: The Pipeline and Storage Segment and Seasonality, in Item 7, MD&A and in Item 8, Financial Statements and Supplementary Data.

The Exploration and Production Segment

The Exploration and Production segment contributed approximately 54.6% of the Company's 2008 net income available for common stock.

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Additional discussion of the Exploration and Production segment appears below under the headings Discontinued Operations, Sources and Availability of Raw Materials and Competition: The Exploration and Production Segment, in Item 7, MD&A and in Item 8, Financial Statements and Supplementary Data.

The Energy Marketing Segment

The Energy Marketing segment contributed approximately 2.2% of the Company's 2008 net income available for common stock.

Additional discussion of the Energy Marketing segment appears below under the headings Sources and Availability of Raw Materials, Competition: The Energy Marketing Segment and Seasonality, in Item 7, MD&A and in Item 8, Financial Statements and Supplementary Data.

The Timber Segment

The Timber segment's contribution to the Company's 2008 net income available for common stock was not significant.

Additional discussion of the Timber segment appears below under the headings Sources and Availability of Raw Materials, Competition: The Timber Segment and Seasonality, in Item 7, MD&A and in Item 8, Financial Statements and Supplementary Data.

All Other Category and Corporate Operations

The All Other category and Corporate operations contributed approximately 0.2% of the Company's 2008 net income available for common stock.

Additional discussion of the All Other category and Corporate operations appears below in Item 7, MD&A and in Item 8, Financial Statements and Supplementary Data.

Discontinued Operations

In August 2007, Seneca sold all of the issued and outstanding shares of SECI. SECI's operations are presented in the Company's financial statements as discontinued operations.

In July 2005, Horizon B.V. sold its entire 85.16% interest in United Energy, a.s. (U.E.), a district heating and electric generation business in the Czech Republic. United Energy's operations are presented in the Company's financial statements as discontinued operations.

Additional discussion of the Company's discontinued operations appears in Item 7, MD&A and in Item 8, Financial Statements and Supplementary Data.

Sources and Availability of Raw Materials

Natural gas is the principal raw material for the Utility segment. In 2008, the Utility segment purchased 76.0 Bcf of gas for core market demand. All such purchases were made from non-affiliated companies. Gas purchased from producers and suppliers in the southwestern United States and Canada under firm contracts (seasonal and longer) accounted for 89% of these purchases. Purchases of gas on the spot market (contracts for one month or less) accounted for 11% of the Utility segment's 2008 purchases. Purchases from Total Gas & Power North America Inc. (18%), Chevron Natural Gas (17%), ConocoPhillips Company (16%) and BP Canada (11%) accounted for 62% of the

Utility's 2008 gas purchases. No other producer or supplier provided the Utility segment with more than 10% of its gas requirements in 2008.

Supply Corporation transports and stores gas owned by its customers, whose gas originates in the southwestern, mid-continent and Appalachian regions of the United States as well as in Canada. Empire transports gas owned by its customers, whose gas originates in the southwestern and mid-continent regions of the United States as well as in Canada. Additional discussion of proposed pipeline projects appears below under Competition: The Pipeline and Storage Segment and in Item 7, MD&A.

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The Exploration and Production segment seeks to discover and produce raw materials (natural gas, oil and hydrocarbon liquids) as further described in this report in Item 7, MD&A and Item 8 at Note J – Business Segment Information and Note O – Supplementary Information for Oil and Gas Producing Activities.

With respect to the Timber segment, Highland requires an adequate supply of timber to process in its sawmill and kiln operations. Fifty-two percent of the timber processed during 2008 in Highland’s sawmill operations came from land owned by the Company’s subsidiaries, and 48% came from outside sources. Timber cut for gas well drilling locations, access roads, and pipelines constituted an increasing portion of Highland’s timber supply, both from land owned by the Company’s subsidiaries and from outside sources. In addition, Highland purchased approximately 5.4 million board feet of green lumber to augment lumber supply for its kiln operations.

The Energy Marketing segment depends on an adequate supply of natural gas to deliver to its customers. In 2008, this segment purchased 57 Bcf of gas, including 56 Bcf for core market demands. The remaining 1 Bcf largely represents gas used in operations. The gas purchased by the Energy Marketing segment originates in either the Appalachian or mid-continent regions of the United States or in Canada.

Competition

Competition in the natural gas industry exists among providers of natural gas, as well as between natural gas and other sources of energy. The natural gas industry has gone through various stages of regulation. Apart from environmental and state utility commission regulation, the natural gas industry has experienced considerable deregulation. This has enhanced the competitive position of natural gas relative to other energy sources, such as fuel oil or electricity, since some of the historical regulatory impediments to adding customers and responding to market forces have been removed. In addition, management believes that the environmental advantages of natural gas have enhanced its competitive position relative to other fuels.

The electric industry has been moving toward a more competitive environment as a result of changes in federal law in 1992 and initiatives undertaken by the FERC and various states. It remains unclear what the impact of any further restructuring in response to legislation or other events may be.

The Company competes on the basis of price, service and reliability, product performance and other factors. Sources and providers of energy, other than those described under this – Competition – heading, do not compete with the Company to any significant extent.

Competition: The Utility Segment

The changes precipitated by the FERC’s restructuring of the natural gas industry in Order No. 636, which was issued in 1992, continue to reshape the roles of the gas utility industry and the state regulatory commissions. In both New York and Pennsylvania, Distribution Corporation has retained substantial numbers of residential and small commercial customers as sales customers. However, for many years almost all the industrial and a substantial number of commercial customers have purchased their gas supplies from marketers and utilized Distribution Corporation’s gas transportation services. Regulators in both New York and Pennsylvania have adopted retail competition programs for natural gas supply purchases by the remaining utility sales customers. To date, the Utility segment’s traditional distribution function remains largely unchanged; however, in New York, the Utility segment has instituted a number of programs to accommodate more widespread customer choice. In Pennsylvania, the PaPUC issued a report in October 2005 that concluded – effective competition – does not exist in the retail natural gas supply market statewide. On September 11, 2008, the PaPUC adopted a Final Order and Action Plan designed to – increase effective competition in the retail market for natural gas services. – The plan sets forth a schedule of action items for utilities and the PaPUC in order to remove – barriers in the market structure – that, in the opinion of the PaPUC, prevented the full participation of

unregulated natural gas suppliers in Pennsylvania retail markets.

Competition for large-volume customers continues with local producers or pipeline companies attempting to sell or transport gas directly to end-users located within the Utility segment's service territories without use of the utility's facilities (i.e., bypass). In addition, competition continues with fuel oil suppliers and may increase with electric utilities making retail energy sales.

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The Utility segment competes in its most vulnerable markets (the large commercial and industrial markets) by offering unbundled, flexible services. The Utility segment continues to develop or promote new sources and uses of natural gas or new services, rates and contracts. The Utility segment also emphasizes and provides high quality service to its customers.

Competition: The Pipeline and Storage Segment

Supply Corporation competes for market growth in the natural gas market with other pipeline companies transporting gas in the northeast United States and with other companies providing gas storage services. Supply Corporation has some unique characteristics which enhance its competitive position. Its facilities are located adjacent to Canada and the northeastern United States and provide part of the link between gas-consuming regions of the eastern United States and gas-producing regions of Canada and the southwestern, southern and other continental regions of the United States. This location offers the opportunity for increased transportation and storage services in the future.

Empire competes for market growth in the natural gas market with other pipeline companies transporting gas in the northeast United States and upstate New York in particular. Empire is well situated to provide transportation from Canadian sourced gas, and its facilities are readily expandable. These characteristics provide Empire the opportunity to compete for an increased share of the gas transportation markets. As noted above, Empire is constructing the Empire Connector project, which will expand its natural gas pipeline and enable Empire to serve new markets in New York and elsewhere in the Northeast. For further discussion of this project, refer to Item 7, MD&A under the headings Investing Cash Flow and Rate and Regulatory Matters.

Competition: The Exploration and Production Segment

The Exploration and Production segment competes with other oil and natural gas producers and marketers with respect to sales of oil and natural gas. The Exploration and Production segment also competes, by competitive bidding and otherwise, with other oil and natural gas producers with respect to exploration and development prospects.

To compete in this environment, Seneca originates and acts as operator on certain of its prospects, seeks to minimize the risk of exploratory efforts through partnership-type arrangements, utilizes technology for both exploratory studies and drilling operations, and seeks market niches based on size, operating expertise and financial criteria.

Competition: The Energy Marketing Segment

The Energy Marketing segment competes with other marketers of natural gas and with other providers of energy supply. Competition in this area is well developed with regard to price and services from local, regional and, more recently, national marketers.

Competition: The Timber Segment

With respect to the Timber segment, Highland competes with other sawmill operations and with other suppliers of timber, logs and lumber. These competitors may be local, regional, national or international in scope. This competition, however, is primarily limited to those entities which either process or supply high quality hardwood species such as cherry, oak and maple as veneer logs, saw logs, export logs or lumber ultimately used in the production of high-end furniture, cabinetry and flooring. The Timber segment sells its products in domestic and international markets.

Seasonality

Variations in weather conditions can materially affect the volume of gas delivered by the Utility segment, as virtually all of its residential and commercial customers use gas for space heating. The effect that this has on Utility segment margins in New York is mitigated by a WNC, which covers the eight-month period from October through May. Weather that is warmer than normal results in a surcharge being added to customers' current bills, while weather that is colder than normal results in a refund being credited to customers' current bills.

Volumes transported and stored by Supply Corporation may vary materially depending on weather, without materially affecting its revenues. Supply Corporation's allowed rates are based on a straight fixed-variable rate

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design which allows recovery of fixed costs in fixed monthly reservation charges. Variable charges based on volumes are designed to recover only the variable costs associated with actual transportation or storage of gas.

Volumes transported by Empire may vary materially depending on weather, which can have a moderate effect on its revenues. Empire's allowed rates currently are based on a modified fixed-variable rate design, which allows recovery of most fixed costs in fixed monthly reservation charges. Variable charges based on volumes are designed to recover variable costs associated with actual transportation of gas, to recover return on equity, and to recover income taxes. When Empire becomes a FERC-regulated interstate pipeline company (which is currently expected to occur in December 2008), Empire's allowed rates, like Supply Corporation's, will be based on a straight fixed-variable design. Under that rate design, weather-related variations in transportation volumes will not materially affect revenues.

Variations in weather conditions materially affect the volume of gas consumed by customers of the Energy Marketing segment. Volume variations have a corresponding impact on revenues within this segment.

The activities of the Timber segment vary on a seasonal basis and are subject to weather constraints. Traditionally, the timber harvesting season occurs when timber growth is dormant and runs from approximately September to March. The operations conducted in the summer months typically focus on pulpwood and on thinning lower-grade or lower value trees from timber stands to encourage the growth of higher-grade or higher value trees.

Capital Expenditures

A discussion of capital expenditures by business segment is included in Item 7, MD&A under the heading "Investing Cash Flow."

Environmental Matters

A discussion of material environmental matters involving the Company is included in Item 7, MD&A under the heading "Environmental Matters" and in Item 8, Note H "Commitments and Contingencies."

Miscellaneous

The Company and its wholly owned or majority-owned subsidiaries had a total of 1,943 full-time employees at September 30, 2008. This is a decrease of approximately one-half of one percent from the 1,952 employees in the Company's U.S. operations at September 30, 2007.

In 2008 the Company entered into new agreements with collective bargaining units in New York. The new agreements went into effect in February 2008 and expire in February 2013. In November 2008 the Company entered into a new agreement with a collective bargaining unit in Pennsylvania. The agreement will go into effect in April 2009 and expire in April 2014. An agreement covering employees in another collective bargaining unit in Pennsylvania is scheduled to expire in May 2009. In November 2008 the Company reached a new agreement with the local leadership of that collective bargaining unit. The members of the collective bargaining unit are scheduled to vote on the agreement in December 2008.

The Utility segment has numerous municipal franchises under which it uses public roads and certain other rights-of-way and public property for the location of facilities. When necessary, the Utility segment renews such franchises.

The Company makes its annual report on Form 10-K, quarterly reports on Form 10-Q, current reports on Form 8-K, and any amendments to those reports, available free of charge on the Company's internet website,

www.nationalfuelgas.com, as soon as reasonably practicable after they are electronically filed with or furnished to the SEC. The information available at the Company's internet website is not part of this Form 10-K or any other report filed with or furnished to the SEC.

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Name and Age (as of November 15, 2008)	Current Company Positions and Other Material Business Experience During Past Five Years
David F. Smith (55)	Chief Executive Officer of the Company since February 2008 and President of the Company since February 2006. Mr. Smith previously served as Chief Operating Officer of the Company from February 2006 through January 2008; President of Supply Corporation from April 2005 through June 2008; President of Empire from April 2005 through January 2008; Vice President of the Company from April 2005 through January 2006; President of Distribution Corporation from July 1999 to April 2005; and Senior Vice President of Supply Corporation from July 2000 to April 2005.
Ronald J. Tanski (56)	Treasurer and Principal Financial Officer of the Company since April 2004; President of Supply Corporation since July 2008. Mr. Tanski previously served as President of Distribution Corporation from February 2006 through June 2008; Treasurer of Distribution Corporation from April 2004 through September 2008; Controller of the Company from February 2003 through March 2004; Senior Vice President of Distribution Corporation from July 2001 through January 2006; and Controller of Distribution Corporation from February 1997 through March 2004.
Matthew D. Cabell (50)	President of Seneca since December 2006. Prior to joining Seneca, Mr. Cabell served as Executive Vice President and General Manager of Marubeni Oil & Gas (USA) Inc., an exploration and production company, from June 2003 to December 2006. From January 2002 to June 2003, Mr. Cabell served as a consultant assisting oil companies in upstream acquisition and divestment transactions as well as Gulf of Mexico entry strategy, first as an independent consultant and then as Vice President of Randall & Dewey, Inc., a major oil and gas transaction advisory firm. Mr. Cabell's prior employers are not subsidiaries or affiliates of the Company.
Anna Marie Cellino (55)	President of Distribution Corporation since July 2008. Ms. Cellino previously served as Secretary of the Company from October 1995 through June 2008; Secretary of Distribution Corporation from September 1999 through September 2008; and Senior Vice President of Distribution Corporation from July 2001 through June 2008.
Karen M. Camiolo (49)	Controller and Principal Accounting Officer of the Company since April 2004; Controller of Distribution Corporation and Supply Corporation since April 2004; and Chief Auditor of the Company from July 1994 through March 2004.
Carl M. Carlotti (53)	Senior Vice President of Distribution Corporation since January 2008. Mr. Carlotti previously served as Vice President of Distribution Corporation from October 1998 to January 2008.
Paula M. Ciprich (48)	Secretary of the Company since July 2008; General Counsel of the Company since January 2005; Secretary of Distribution Corporation since July 2008. Ms. Ciprich previously served as General Counsel of Distribution Corporation from February 1997 through February 2007 and as Assistant Secretary of Distribution Corporation from February 1997 through June 2008.

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Donna L. DeCarolis (49)	Vice President Business Development of the Company since October 2007. Ms. DeCarolis previously served as President of NFR from January 2005 to October 2007; Secretary of NFR from March 2002 to October 2007; and Vice President of NFR from May 2001 to January 2005.
John R. Pustulka (56)	Senior Vice President of Supply Corporation since July 2001.
James D. Ramsdell (53)	Senior Vice President of Distribution Corporation since July 2001.

- (1) The executive officers serve at the pleasure of the Board of Directors. The information provided relates to the Company and its principal subsidiaries. Many of the executive officers also have served or currently serve as officers or directors of other subsidiaries of the Company.

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Item 1A Risk Factors

As a holding company, National Fuel depends on its operating subsidiaries to meet its financial obligations.

National Fuel is a holding company with no significant assets other than the stock of its operating subsidiaries. In order to meet its financial needs, National Fuel relies exclusively on repayments of principal and interest on intercompany loans made by National Fuel to its operating subsidiaries and income from dividends and other cash flow from the subsidiaries. Such operating subsidiaries may not generate sufficient net income to pay upstream dividends or generate sufficient cash flow to make payments of principal or interest on such intercompany loans.

Recent disruptions in financial markets may affect National Fuel's ability to obtain financing or refinance maturing debt on reasonable terms and may have other adverse effects.

Widely-documented disruptions in financial markets have resulted in a severe tightening of credit availability in the United States. Liquidity in credit markets has contracted significantly, making terms for certain financings less attractive. Ongoing turmoil in the credit markets may make it difficult for National Fuel to obtain financing on acceptable terms or at all for working capital, capital expenditures and other investments and to refinance maturing debt on favorable terms. These difficulties could adversely affect National Fuel's operations and financial performance.

National Fuel is dependent on bank credit facilities and continued access to capital markets to successfully execute its operating strategies.

In addition to its longer term debt that is issued to the public under its indentures, National Fuel relies upon shorter term bank borrowings and commercial paper to finance a portion of its operations. National Fuel is dependent on these capital sources to provide capital to its subsidiaries to allow them to acquire, maintain and develop their properties. The availability and cost of these credit sources is cyclical and these capital sources may not remain available to National Fuel or National Fuel may not be able to obtain money at a reasonable cost in the future. Recent access to the commercial paper markets has been on less favorable terms as a result of ongoing turmoil in the credit markets, and the commercial paper markets may not consistently be a reliable source of short-term financing for National Fuel in the future. National Fuel's ability to borrow under its credit facilities and commercial paper agreements depends on National Fuel's compliance with its obligations under the facilities and agreements. In addition, all of National Fuel's short-term bank loans are in the form of floating rate debt or debt that may have rates fixed for very short periods of time. At present, National Fuel has no active interest rate hedges in place to protect against interest rate fluctuations on short-term bank debt. In addition, the interest rates on National Fuel's short-term bank loans and the ability of National Fuel to issue commercial paper are affected by its debt credit ratings published by Standard & Poor's Ratings Service (S&P), Moody's Investors Service and Fitch Ratings Service. On October 15, 2008, National Fuel's senior unsecured credit rating of BBB+ was placed on CreditWatch-with negative implications by S&P. A ratings downgrade could increase the interest cost of debt issued by National Fuel and decrease future availability of money from banks, commercial paper purchasers and other sources. National Fuel's debt securities are currently rated at investment grade and the Company believes it is important to maintain investment grade credit ratings to conduct its business.

National Fuel may be adversely affected by economic conditions and their impact on our suppliers and customers.

Periods of slowed economic activity generally result in decreased energy consumption, particularly by industrial and large commercial companies. As a consequence, national or regional recessions or other downturns in economic activity could adversely affect National Fuel's revenues and cash flows or restrict its future growth. Economic conditions in National Fuel's utility service territories and energy marketing territories also impact its collections of accounts receivable. All of National Fuel's segments are exposed to risks associated with the creditworthiness or performance of key suppliers and customers, many of which may be adversely affected by volatile conditions in the

financial markets. These conditions could result in financial

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instability or other adverse effects at any of our suppliers or customers. For example, counterparties to National Fuel's commodity hedging arrangements might not be able to perform their obligations under these arrangements. Customers of National Fuel's Utility and Energy Marketing segments may have particular trouble paying their bills during periods of declining economic activity and high commodity prices, potentially resulting in increased bad debt expense and reduced earnings. Any of these events could have a material adverse effect on National Fuel's results of operations, financial condition and cash flows.

The increasing costs of certain employee and retiree benefits could adversely affect National Fuel's results.

National Fuel's earnings and cash flow may be impacted by the amount of income or expense it expends or records for employee benefit plans. This is particularly true for pension plans, which are dependent on actual plan asset returns and factors used to determine the value and current costs of plan benefit obligations. In addition, if medical costs rise at a rate faster than the general inflation rate, National Fuel might not be able to mitigate the rising costs of medical benefits. Increases to the costs of pension and medical benefits could have an adverse effect on National Fuel's financial results.

National Fuel's credit ratings may not reflect all the risks of an investment in its securities.

National Fuel's credit ratings are an independent assessment of its ability to pay its obligations. Consequently, real or anticipated changes in the Company's credit ratings will generally affect the market value of the specific debt instruments that are rated, as well as the market value of the Company's common stock. National Fuel's credit ratings, however, may not reflect the potential impact on the value of its common stock of risks related to structural, market or other factors discussed in this Form 10-K.

National Fuel's need to comply with comprehensive, complex, and sometimes unpredictable government regulations may increase its costs and limit its revenue growth, which may result in reduced earnings.

While National Fuel generally refers to its Utility segment and its Pipeline and Storage segment as its regulated segments, there are many governmental regulations that have an impact on almost every aspect of National Fuel's businesses. Existing statutes and regulations may be revised or reinterpreted and new laws and regulations may be adopted or become applicable to the Company, which may affect its business in ways that the Company cannot predict.

In its Utility segment, the operations of Distribution Corporation are subject to the jurisdiction of the NYPSC and the PaPUC. The NYPSC and the PaPUC, among other things, approve the rates that Distribution Corporation may charge to its utility customers. Those approved rates also impact the returns that Distribution Corporation may earn on the assets that are dedicated to those operations. If Distribution Corporation is required in a rate proceeding to reduce the rates it charges its utility customers, or if Distribution Corporation is unable to obtain approval for rate increases from these regulators, particularly when necessary to cover increased costs (including costs that may be incurred in connection with governmental investigations or proceedings or mandated infrastructure inspection, maintenance or replacement programs), earnings may decrease.

In addition to their historical methods of utility regulation, both the PaPUC and NYPSC have sought to establish competitive markets in which customers may purchase supplies of gas from marketers, rather than from utility companies. In June 1999, the Governor of Pennsylvania signed into law the Natural Gas Choice and Competition Act. The Act revised the Public Utility Code relating to the restructuring of the natural gas industry, to permit consumer choice of natural gas suppliers. The early programs instituted to comply with the Act did not result in significant change, and many residential customers currently continue to purchase natural gas from the utility companies. In October 2005, the PaPUC concluded that effective competition does not exist in the retail natural gas supply market

statewide. On September 11, 2008, the PaPUC adopted a Final Order and Action Plan designed to increase effective competition in the retail market for natural gas services. The plan sets forth a schedule of action items for utilities and the PaPUC in order to remove barriers in the market structure that, in the opinion of the PaPUC, prevented the full participation of unregulated natural gas

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suppliers in Pennsylvania retail markets. In New York, in August 2004, the NYPSC issued its Statement of Policy on Further Steps Toward Competition in Retail Energy Markets. This policy statement has a similar goal of encouraging customer choice of alternative natural gas providers. In 2005, the NYPSC stepped up its efforts to encourage customer choice at the retail residential level, and customer choice activities increased in Distribution Corporation's New York service territory. In April 2007, the NYPSC, noting that the retail energy marketplace in New York is established and continuing to expand, commenced a review to determine if existing programs initially designed to promote competition had outlived their usefulness and whether the cost of programs currently funded by utility rate payers should be shifted to market competitors. Increased retail choice activities, to the extent they occur, may increase Distribution Corporation's cost of doing business, put an additional portion of its business at regulatory risk, and create uncertainty for the future, all of which may make it more difficult to manage Distribution Corporation's business profitably.

Both the NYPSC and the PaPUC have instituted proceedings for the purpose of promoting conservation of energy commodities, including natural gas. In New York, Distribution Corporation implemented a Conservation Incentive Program that promotes conservation and efficient use of natural gas by offering customer rebates for high-efficiency appliances, among other things. The intent of conservation and efficiency programs is to reduce customer usage of natural gas. Under traditional volumetric rates, reduced usage by customers results in decreased revenues to the Utility. To prevent revenue erosion caused by conservation, the NYPSC approved a revenue decoupling mechanism that renders Distribution Corporation's New York division financially indifferent to the effects of conservation. In Pennsylvania, although a proceeding is pending, the PaPUC has not yet directed Distribution Corporation to implement conservation measures. If the NYPSC were to revoke the revenue decoupling mechanism in a future proceeding or the PaPUC were to adopt a conservation program without a revenue decoupling mechanism or other changes in rate design, reduced customer usage could decrease revenues, forcing Distribution Corporation to file for rate relief.

In its Pipeline and Storage segment, National Fuel is subject to the jurisdiction of the FERC with respect to Supply Corporation, and to the jurisdiction of the NYPSC with respect to Empire. The FERC has authorized Empire to construct and operate the Empire Connector project. When Empire completes construction and commences operations of the Empire Connector, Empire will at that time become a FERC-regulated pipeline company. The FERC and the NYPSC, among other things, approve the rates that Supply Corporation and Empire, respectively, may charge to their natural gas transportation and/or storage customers. Those approved rates also impact the returns that Supply Corporation and Empire may earn on the assets that are dedicated to those operations. State commissions can also petition the FERC to investigate whether Supply Corporation's rates are still just and reasonable, and if not, to reduce those rates prospectively. If Supply Corporation or Empire is required in a rate proceeding to reduce the rates it charges its natural gas transportation and/or storage customers, or if Supply Corporation or Empire is unable to obtain approval for rate increases, particularly when necessary to cover increased costs, Supply Corporation's or Empire's earnings may decrease.

National Fuel's liquidity, and in certain circumstances, its earnings, could be adversely affected by the cost of purchasing natural gas during periods in which natural gas prices are rising significantly.

Tariff rate schedules in each of the Utility segment's service territories contain purchased gas adjustment clauses which permit Distribution Corporation to file with state regulators for rate adjustments to recover increases in the cost of purchased gas. Assuming those rate adjustments are granted, increases in the cost of purchased gas have no direct impact on profit margins. Nevertheless, increases in the cost of purchased gas affect cash flows and can therefore impact the amount or availability of National Fuel's capital resources. National Fuel has issued commercial paper and used short-term borrowings in the past to temporarily finance storage inventories and purchased gas costs, and although National Fuel expects to do so in the future, it may not be able to access the markets for such borrowings at attractive interest rates or at all. Distribution Corporation is required to file an accounting reconciliation with the

regulators in each of the Utility segment's service territories regarding the costs of purchased gas. Due to the nature of the regulatory process, there is a risk of a disallowance of full recovery of these costs during any period in which there has been a substantial upward spike in these costs. Any material disallowance of purchased gas costs could have a material adverse effect on cash flow and earnings. In addition, even when Distribution Corporation is allowed full recovery of these purchased

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gas costs, during periods when natural gas prices are significantly higher than historical levels, customers may have trouble paying the resulting higher bills, and Distribution Corporation's bad debt expenses may increase and ultimately reduce earnings.

Changes in interest rates may affect National Fuel's ability to finance capital expenditures and to refinance maturing debt.

National Fuel's ability to finance capital expenditures and to refinance maturing debt will depend in part upon interest rates. The direction in which interest rates may move is uncertain. Declining interest rates have generally been believed to be favorable to utilities, while rising interest rates are generally believed to be unfavorable, because of the levels of debt that utilities may have outstanding. In addition, National Fuel's authorized rate of return in its regulated businesses is based upon certain assumptions regarding interest rates. If interest rates are lower than assumed rates, National Fuel's authorized rate of return could be reduced. If interest rates are higher than assumed rates, National Fuel's ability to earn its authorized rate of return may be adversely impacted.

Decreased oil and natural gas prices could adversely affect revenues, cash flows and profitability.

National Fuel's exploration and production operations are materially dependent on prices received for its oil and natural gas production. Both short-term and long-term price trends affect the economics of exploring for, developing, producing, gathering and processing oil and natural gas. Oil and natural gas prices can be volatile and can be affected by: weather conditions, including natural disasters; the supply and price of foreign oil and natural gas; the level of consumer product demand; national and worldwide economic conditions, including economic disruptions caused by terrorist activities, acts of war or major accidents; political conditions in foreign countries; the price and availability of alternative fuels; the proximity to, and availability of capacity on transportation facilities; regional levels of supply and demand; energy conservation measures; and government regulations, such as regulation of natural gas transportation, royalties, and price controls. National Fuel sells most of its oil and natural gas at current market prices rather than through fixed-price contracts, although as discussed below, National Fuel frequently hedges the price of a significant portion of its future production in the financial markets. The prices National Fuel receives depend upon factors beyond National Fuel's control, including the factors affecting price mentioned above. National Fuel believes that any prolonged reduction in oil and natural gas prices would restrict its ability to continue the level of exploration and production activity National Fuel otherwise would pursue, which could have a material adverse effect on its revenues, cash flows and results of operations.

National Fuel has significant transactions involving price hedging of its oil and natural gas production as well as its fixed price purchase and sale commitments.

In order to protect itself to some extent against unusual price volatility and to lock in fixed pricing on oil and natural gas production for certain periods of time, National Fuel periodically enters into commodity price derivatives contracts (hedging arrangements) with respect to a portion of its expected production. These contracts may at any time cover as much as approximately 80% of National Fuel's expected energy production during the upcoming 12-month period. These contracts reduce exposure to subsequent price drops but can also limit National Fuel's ability to benefit from increases in commodity prices. In addition, the Energy Marketing segment enters into certain hedging arrangements, primarily with respect to its fixed price purchase and sales commitments and its volumes of gas stored underground. National Fuel's Pipeline and Storage segment enters into hedging arrangements with respect to certain sales of efficiency gas, and the All Other category has hedging arrangements in place with respect to certain volumes of landfill gas committed for sale.

Under applicable accounting rules, the Company's hedging arrangements are subject to quarterly effectiveness tests. Inherent within those effectiveness tests are assumptions concerning the long-term price differential between different

types of crude oil, assumptions concerning the difference between published natural gas price indexes established by pipelines in which hedged natural gas production is delivered and the reference price established in the hedging arrangements, assumptions regarding the levels of production that will be achieved and, with regard to fixed price commitments, assumptions regarding the creditworthiness of

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certain customers and their forecasted consumption of natural gas. Depending on market conditions for natural gas and crude oil and the levels of production actually achieved, it is possible that certain of those assumptions may change in the future, and, depending on the magnitude of any such changes, it is possible that a portion of the Company's hedges may no longer be considered highly effective. In that case, gains or losses from the ineffective derivative financial instruments would be marked-to-market on the income statement without regard to an underlying physical transaction. Gains would occur to the extent that natural gas and crude oil hedge prices exceed market prices for the Company's natural gas and crude oil production, and losses would occur to the extent that market prices for the Company's natural gas and crude oil production exceed hedge prices.

Use of energy commodity price hedges also exposes National Fuel to the risk of non-performance by a contract counterparty. These parties might not be able to perform their obligations under the hedge arrangements.

It is National Fuel's policy that the use of commodity derivatives contracts comply with various restrictions in effect in respective business segments. For example, in the Exploration and Production segment, commodity derivatives contracts must be confined to the price hedging of existing and forecast production, and in the Energy Marketing segment, commodity derivatives with respect to fixed price purchase and sales commitments must be matched against commitments reasonably certain to be fulfilled. Similar restrictions apply in the Pipeline and Storage segment and the All Other category. National Fuel maintains a system of internal controls to monitor compliance with its policy. However, unauthorized speculative trades, if they were to occur, could expose National Fuel to substantial losses to cover positions in its derivatives contracts. In addition, in the event the Company's actual production of oil and natural gas falls short of hedged forecast production, the Company may incur substantial losses to cover its hedges.

You should not place undue reliance on reserve information because such information represents estimates.

This Form 10-K contains estimates of National Fuel's proved oil and natural gas reserves and the future net cash flows from those reserves that were prepared by National Fuel's petroleum engineers and audited by independent petroleum engineers. Petroleum engineers consider many factors and make assumptions in estimating National Fuel's oil and natural gas reserves and future net cash flows. These factors include: historical production from the area compared with production from other producing areas; the assumed effect of governmental regulation; and assumptions concerning oil and natural gas prices, production and development costs, severance and excise taxes, and capital expenditures. Lower oil and natural gas prices generally cause estimates of proved reserves to be lower. Estimates of reserves and expected future cash flows prepared by different engineers, or by the same engineers at different times, may differ substantially. Ultimately, actual production, revenues and expenditures relating to National Fuel's reserves will vary from any estimates, and these variations may be material. Accordingly, the accuracy of National Fuel's reserve estimates is a function of the quality of available data and of engineering and geological interpretation and judgment.

If conditions remain constant, then National Fuel is reasonably certain that its reserve estimates represent economically recoverable oil and natural gas reserves and future net cash flows. If conditions change in the future, then subsequent reserve estimates may be revised accordingly. You should not assume that the present value of future net cash flows from National Fuel's proved reserves is the current market value of National Fuel's estimated oil and natural gas reserves. In accordance with SEC requirements, National Fuel bases the estimated discounted future net cash flows from its proved reserves on prices and costs as of the date of the estimate. Actual future prices and costs may differ materially from those used in the net present value estimate. Any significant price changes will have a material effect on the present value of National Fuel's reserves.

Petroleum engineering is a subjective process of estimating underground accumulations of natural gas and other hydrocarbons that cannot be measured in an exact manner. The process of estimating oil and natural gas reserves is complex. The process involves significant decisions and assumptions in the evaluation of available geological,

geophysical, engineering and economic data for each reservoir. Future economic and operating conditions are uncertain, and changes in those conditions could cause a revision to National Fuel's reserve

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estimates in the future. Estimates of economically recoverable oil and natural gas reserves and of future net cash flows depend upon a number of variable factors and assumptions, including historical production from the area compared with production from other comparable producing areas, and the assumed effects of regulations by governmental agencies. Because all reserve estimates are to some degree subjective, each of the following items may differ materially from those assumed in estimating reserves: the quantities of oil and natural gas that are ultimately recovered, the timing of the recovery of oil and natural gas reserves, the production and operating costs incurred, the amount and timing of future development and abandonment expenditures, and the price received for the production.

The amount and timing of actual future oil and natural gas production and the cost of drilling are difficult to predict and may vary significantly from reserves and production estimates, which may reduce National Fuel's earnings.

There are many risks in developing oil and natural gas, including numerous uncertainties inherent in estimating quantities of proved oil and natural gas reserves and in projecting future rates of production and timing of development expenditures. The future success of National Fuel's Exploration and Production segment depends on its ability to develop additional oil and natural gas reserves that are economically recoverable, and its failure to do so may reduce National Fuel's earnings. The total and timing of actual future production may vary significantly from reserves and production estimates. National Fuel's drilling of development wells can involve significant risks, including those related to timing, success rates, and cost overruns, and these risks can be affected by lease and rig availability, geology, and other factors. Drilling for oil and natural gas can be unprofitable, not only from non-productive wells, but from productive wells that do not produce sufficient revenues to return a profit. Also, title problems, weather conditions, governmental requirements, and shortages or delays in the delivery of equipment and services can delay drilling operations or result in their cancellation. The cost of drilling, completing, and operating wells is often uncertain, and new wells may not be productive or National Fuel may not recover all or any portion of its investment. Without continued successful exploitation or acquisition activities, National Fuel's reserves and revenues will decline as a result of its current reserves being depleted by production. National Fuel cannot assure you that it will be able to find or acquire additional reserves at acceptable costs.

Financial accounting requirements regarding exploration and production activities may affect National Fuel's profitability.

National Fuel accounts for its exploration and production activities under the full cost method of accounting. Each quarter, National Fuel must compare the level of its unamortized investment in oil and natural gas properties to the present value of the future net revenue projected to be recovered from those properties according to methods prescribed by the SEC. In determining present value, the Company uses quarter-end spot prices for oil and natural gas (as adjusted for hedging). If, at the end of any quarter, the amount of the unamortized investment exceeds the net present value of the projected future cash flows, such investment may be considered to be impaired, and the full cost accounting rules require that the investment must be written down to the calculated net present value. Such an instance would require National Fuel to recognize an immediate expense in that quarter, and its earnings would be reduced. National Fuel's Exploration and Production segment last recorded an impairment charge under the full cost method of accounting in 2006. Because of the variability in National Fuel's investment in oil and natural gas properties and the volatile nature of commodity prices, National Fuel cannot predict when in the future it may again be affected by such an impairment calculation.

Environmental regulation significantly affects National Fuel's business.

National Fuel's business operations are subject to federal, state, and local laws and regulations relating to environmental protection. These laws and regulations concern the generation, storage, transportation, disposal or discharge of contaminants into the environment and the general protection of public health, natural resources, wildlife

and the environment. Costs of compliance and liabilities could negatively affect National Fuel's results of operations, financial condition and cash flows. In addition, compliance with environmental

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laws and regulations could require unexpected capital expenditures at National Fuel's facilities. Because the costs of complying with environmental regulations are significant, additional regulation could negatively affect National Fuel's business. Although National Fuel cannot predict the impact of the interpretation or enforcement of EPA standards or other federal, state and local regulations, National Fuel's costs could increase if environmental laws and regulations become more strict.

The nature of National Fuel's operations presents inherent risks of loss that could adversely affect its results of operations, financial condition and cash flows.

National Fuel's operations in its various segments are subject to inherent hazards and risks such as: fires; natural disasters; explosions; geological formations with abnormal pressures; blowouts during well drilling; collapses of wellbore casing or other tubulars; pipeline ruptures; spills; and other hazards and risks that may cause personal injury, death, property damage, environmental damage or business interruption losses. Additionally, National Fuel's facilities, machinery, and equipment may be subject to sabotage. Any of these events could cause a loss of hydrocarbons, environmental pollution, claims for personal injury, death, property damage or business interruption, or governmental investigations, recommendations, claims, fines or penalties. As protection against operational hazards, National Fuel maintains insurance coverage against some, but not all, potential losses. In addition, many of the agreements that National Fuel executes with contractors provide for the division of responsibilities between the contractor and National Fuel, and National Fuel seeks to obtain an indemnification from the contractor for certain of these risks. National Fuel is not always able, however, to secure written agreements with its contractors that contain indemnification, and sometimes National Fuel is required to indemnify others.

Insurance or indemnification agreements when obtained may not adequately protect National Fuel against liability from all of the consequences of the hazards described above. The occurrence of an event not fully insured or indemnified against, the imposition of fines, penalties or mandated programs by governmental authorities, the failure of a contractor to meet its indemnification obligations, or the failure of an insurance company to pay valid claims could result in substantial losses to National Fuel. In addition, insurance may not be available, or if available may not be adequate, to cover any or all of these risks. It is also possible that insurance premiums or other costs may rise significantly in the future, so as to make such insurance prohibitively expensive.

Due to the significant cost of insurance coverage for named windstorms in the Gulf of Mexico, National Fuel determined that it was not economical to purchase insurance to fully cover its exposures related to such storms. It is possible that named windstorms in the Gulf of Mexico could have a material adverse effect on National Fuel's results of operations, financial condition and cash flows.

Hazards and risks faced by National Fuel, and insurance and indemnification obtained or provided by National Fuel, may subject National Fuel to litigation or administrative proceedings from time to time. Such litigation or proceedings could result in substantial monetary judgments, fines or penalties against National Fuel or be resolved on unfavorable terms, the result of which could have a material adverse effect on National Fuel's results of operations, financial condition and cash flows.

Significant shareholders or potential shareholders may attempt to effect changes at National Fuel or acquire control over National Fuel, which could adversely affect National Fuel's results of operations and financial condition.

In January 2008, National Fuel entered into an agreement with New Mountain Vantage GP, L.L.C. (New Mountain) and certain parties related to New Mountain, including the California Public Employees' Retirement System (collectively, Vantage), to settle a proxy contest pertaining to the election of directors to National Fuel's Board of Directors at National Fuel's 2008 Annual Meeting of Stockholders. Pursuant to the settlement agreement, National

Fuel and Vantage agreed, among other things, to a standstill whereby, until September 2009, Vantage will not, among other things, acquire voting securities that would increase its beneficial ownership to more than 9.6% of National Fuel's voting securities; engage in any proxy solicitations or advance any shareholder proposals; attempt to control National Fuel's Board of Directors, management or

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policies; call a meeting of shareholders; obtain additional representation to the Board of Directors; or effect the removal of any member of the Board of Directors. At the end of the standstill period, Vantage may again seek to effect changes at National Fuel or acquire control over National Fuel. In addition, other existing or potential shareholders may engage in proxy solicitations, advance shareholder proposals or otherwise attempt to effect changes or acquire control over National Fuel.

Campaigns by shareholders to effect changes at publicly traded companies are sometimes led by investors seeking to increase short-term shareholder value through actions such as changes in strategy or management, changes to the board of directors, restructuring, increased financial leverage, special dividends, stock repurchases or sales of assets or the entire company. Responding to proxy contests and other actions by activist shareholders can be costly and time-consuming, disrupting National Fuel's operations and diverting the attention of National Fuel's Board of Directors and senior management. As a result, shareholder campaigns could adversely affect National Fuel's results of operations and financial condition.

Item 1B *Unresolved Staff Comments*

None

Item 2 *Properties*

General Information on Facilities

The net investment of the Company in property, plant and equipment was \$3.2 billion at September 30, 2008. Approximately 62% of this investment was in the Utility and Pipeline and Storage segments, which are primarily located in western and central New York and northwestern Pennsylvania. The Exploration and Production segment, which has the next largest investment in net property, plant and equipment (35%), is primarily located in California, in the Appalachian region of the United States, in Wyoming, and in the Gulf Coast region of Texas, Louisiana, and Alabama. The remaining net investment in property, plant and equipment consisted of the Timber segment (2%) which is located primarily in northwestern Pennsylvania, and All Other and Corporate operations (1%). During the past five years, the Company has made additions to property, plant and equipment in order to expand and improve transmission and distribution facilities for both retail and transportation customers. Net property, plant and equipment has increased \$163.1 million, or 5.5%, since 2003. During 2007, the Company sold SECI, Seneca's wholly owned subsidiary that operated in Canada. The net property, plant and equipment of SECI at the date of sale was \$107.7 million. In addition, during 2005, the Company sold its majority interest in U.E., a district heating and electric generation business in the Czech Republic. The net property, plant and equipment of U.E. at the date of sale was \$223.9 million.

The Utility segment had a net investment in property, plant and equipment of \$1.1 billion at September 30, 2008. The net investment in its gas distribution network (including 14,819 miles of distribution pipeline) and its service connections to customers represent approximately 52% and 34%, respectively, of the Utility segment's net investment in property, plant and equipment at September 30, 2008.

The Pipeline and Storage segment had a net investment of \$826.5 million in property, plant and equipment at September 30, 2008. Transmission pipeline represents 27% of this segment's total net investment and includes 2,371 miles of pipeline utilized to move large volumes of gas throughout its service area. Storage facilities represent 21% of this segment's total net investment and consist of 31 storage fields, four of which are jointly owned and operated with certain pipeline suppliers, and 429 miles of pipeline. Net investment in storage facilities includes \$94.8 million of gas stored underground-noncurrent, representing the cost of the gas utilized to maintain pressure levels for normal operating purposes as well as gas maintained for system balancing and other purposes, including that

needed for no-notice transportation service. The Pipeline and Storage segment has 27 compressor stations with 75,104 installed compressor horsepower that represent 11% of this segment's total net investment in property, plant and equipment.

The Exploration and Production segment had a net investment in property, plant and equipment of \$1.1 billion at September 30, 2008.

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The Timber segment had a net investment in property, plant and equipment of \$86.4 million at September 30, 2008. Located primarily in northwestern Pennsylvania, the net investment includes two sawmills, 103,680 acres of land and timber, and 3,122 acres of timber rights.

The Utility and Pipeline and Storage segments' facilities provided the capacity to meet the Company's 2008 peak day sendout, including transportation service, of 1,632 MMcf, which occurred on February 10, 2008. Withdrawals from storage of 768.3 MMcf provided approximately 47.1% of the requirements on that day.

Company maps are included in exhibit 99.2 of this Form 10-K and are incorporated herein by reference.

Exploration and Production Activities

The Company is engaged in the exploration for, and the development and purchase of, natural gas and oil reserves in California, in the Appalachian region of the United States, in Wyoming, and in the Gulf Coast region of Texas, Louisiana, and Alabama. Also, Exploration and Production operations were conducted in the provinces of Alberta, Saskatchewan and British Columbia in Canada, until the sale of these properties on August 31, 2007. Further discussion of the sale of the Canadian oil and gas properties is included in Item 8, Note I - Discontinued Operations. Further discussion of oil and gas producing activities is included in Item 8, Note O - Supplementary Information for Oil and Gas Producing Activities. Note O sets forth proved developed and undeveloped reserve information for Seneca. Seneca's proved developed and undeveloped natural gas reserves increased from 205 Bcf at September 30, 2007 to 226 Bcf at September 30, 2008. This increase is attributed primarily to extensions and discoveries (40.1 Bcf), primarily in the Appalachian region (31.3 Bcf). This increase was partially offset by production of 22.3 Bcf. Seneca's proved developed and undeveloped oil reserves decreased from 47,586 Mbbbl at September 30, 2007 to 46,198 Mbbbl at September 30, 2008. This decrease is attributed to production (3,070 Mbbbl), primarily occurring in California (2,460 Mbbbl) and sales of minerals in place (1,334 Mbbbl). These decreases were partially offset by purchases of minerals in place (2,084 Mbbbl) and extensions and discoveries (827 Mbbbl). On a Bcfe basis, Seneca's proved developed and undeveloped reserves increased from 491 Bcfe at September 30, 2007 to 503 Bcfe at September 30, 2008. Seneca's proved developed and undeveloped natural gas reserves decreased from 233 Bcf at September 30, 2006 to 205 Bcf at September 30, 2007. This decrease is attributed primarily to the sale of the Canadian gas properties (40.1 Bcf) and production of 26.3 Bcf. These decreases were partially offset by extensions and discoveries of 34.6 Bcf, primarily in the Appalachian region (29.7 Bcf). Seneca's proved developed and undeveloped oil reserves decreased from 58,018 Mbbbl at September 30, 2006 to 47,586 Mbbbl at September 30, 2007. This decrease is attributed to revisions of previous estimates (5,963 Mbbbl), primarily occurring in California, production (3,450 Mbbbl) and the sale of the Canadian oil properties (1,458 Mbbbl). On a Bcfe basis, Seneca's proved developed and undeveloped reserves decreased from 581 Bcfe at September 30, 2006 to 491 Bcfe at September 30, 2007.

Seneca's oil and gas reserves reported in Item 8 at Note O as of September 30, 2008 were estimated by Seneca's geologists and engineers and were audited by independent petroleum engineers from Netherland, Sewell & Associates, Inc. Seneca reports its oil and gas reserve information on an annual basis to the Energy Information Administration (EIA), a statistical agency of the U.S. Department of Energy. The oil and gas reserve information reported to the EIA showed 204 Bcf and 49,899 Mbbbl of gas and oil reserves, respectively, which differs from the reserve information summarized in Item 8 at Note O. The reasons for this difference are as follows: (a) reserves are reported to the EIA on a calendar year basis, while reserves disclosed in Item 8 at Note O are shown on a fiscal year basis; (b) reserves reported to the EIA include only properties operated by Seneca, while reserves disclosed in Item 8 at Note O included both Seneca operated properties and non-operated properties in which Seneca has an interest; and (c) reserves are reported to the EIA on a gross basis versus the reserves disclosed in Item 8 at Note O, which are reported on a net revenue interest basis.

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The following is a summary of certain oil and gas information taken from Seneca's records. All monetary amounts are expressed in U.S. dollars.

Production

	For The Year Ended September 30		
	2008	2007	2006
United States			
Gulf Coast Region			
Average Sales Price per Mcf of Gas	\$ 10.03	\$ 6.58	\$ 8.01
Average Sales Price per Barrel of Oil	\$ 107.27	\$ 63.04	\$ 64.10
Average Sales Price per Mcf of Gas (after hedging)	\$ 9.49	\$ 6.87	\$ 5.89
Average Sales Price per Barrel of Oil (after hedging)	\$ 98.56	\$ 64.09	\$ 47.46
Average Production (Lifting) Cost per Mcf Equivalent of Gas and Oil Produced	\$ 1.63	\$ 1.08	\$ 0.86
Average Production per Day (in MMcf Equivalent of Gas and Oil Produced)	38	40	36
West Coast Region			
Average Sales Price per Mcf of Gas	\$ 8.71	\$ 6.54	\$ 7.93
Average Sales Price per Barrel of Oil	\$ 98.17	\$ 56.86	\$ 56.80
Average Sales Price per Mcf of Gas (after hedging)	\$ 8.22	\$ 6.82	\$ 7.19
Average Sales Price per Barrel of Oil (after hedging)	\$ 77.64	\$ 47.43	\$ 37.69
Average Production (Lifting) Cost per Mcf Equivalent of Gas and Oil Produced	\$ 2.01	\$ 1.54	\$ 1.35
Average Production per Day (in MMcf Equivalent of Gas and Oil Produced)	51	50	53
Appalachian Region			
Average Sales Price per Mcf of Gas	\$ 9.73	\$ 7.48	\$ 9.53
Average Sales Price per Barrel of Oil	\$ 97.40	\$ 62.26	\$ 65.28
Average Sales Price per Mcf of Gas (after hedging)	\$ 8.85	\$ 8.25	\$ 8.90
Average Sales Price per Barrel of Oil (after hedging)	\$ 97.40	\$ 62.26	\$ 65.28
Average Production (Lifting) Cost per Mcf Equivalent of Gas and Oil Produced	\$ 0.77	\$ 0.69	\$ 0.69
Average Production per Day (in MMcf Equivalent of Gas and Oil Produced)	22	17	15
Total United States			
Average Sales Price per Mcf of Gas	\$ 9.70	\$ 6.82	\$ 8.42
Average Sales Price per Barrel of Oil	\$ 99.64	\$ 58.43	\$ 58.47
Average Sales Price per Mcf of Gas (after hedging)	\$ 9.05	\$ 7.25	\$ 7.02
Average Sales Price per Barrel of Oil (after hedging)	\$ 81.75	\$ 51.68	\$ 40.26
Average Production (Lifting) Cost per Mcf Equivalent of Gas and Oil Produced	\$ 1.64	\$ 1.23	\$ 1.09
Average Production per Day (in MMcf Equivalent of Gas and Oil Produced)	111	108	104

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	For The Year Ended September 30		
	2008	2007	2006
Canada Discontinued Operations			
Average Sales Price per Mcf of Gas	\$	\$ 6.09	\$ 7.14
Average Sales Price per Barrel of Oil	\$	\$ 50.06	\$ 51.40
Average Sales Price per Mcf of Gas (after hedging)	\$	\$ 6.17	\$ 7.47
Average Sales Price per Barrel of Oil (after hedging)	\$	\$ 50.06	\$ 51.40
Average Production (Lifting) Cost per Mcf Equivalent of Gas and Oil Produced	\$	\$ 1.94	\$ 1.57
Average Production per Day (in MMcf Equivalent of Gas and Oil Produced)		21	26
Total Company			
Average Sales Price per Mcf of Gas	\$ 9.70	\$ 6.64	\$ 8.04
Average Sales Price per Barrel of Oil	\$ 99.64	\$ 57.93	\$ 57.94
Average Sales Price per Mcf of Gas (after hedging)	\$ 9.05	\$ 6.98	\$ 7.15
Average Sales Price per Barrel of Oil (after hedging)	\$ 81.75	\$ 51.58	\$ 41.10
Average Production (Lifting) Cost per Mcf Equivalent of Gas and Oil Produced	\$ 1.64	\$ 1.35	\$ 1.18
Average Production per Day (in MMcf Equivalent of Gas and Oil Produced)	111	129	130

Productive Wells

		Gulf Coast Region		West Coast Region		Appalachian Region		Total Company	
At September 30, 2008		Gas	Oil	Gas	Oil	Gas	Oil	Gas	Oil
Productive Wells	Gross	25	42	1,437	2,641	6	2,666	1,485	1,485
Productive Wells	Net	14	14	1,426	2,570	5	2,584	1,445	1,445

Developed and Undeveloped Acreage

At September 30, 2008		Gulf Coast Region	West Coast Region	Appalachian Region	Total Company
Developed Acreage					
Gross		113,934	11,360	531,743	657,037
Net		80,852	10,945	501,411	593,208
Undeveloped Acreage					
Gross		142,118		458,894	601,012
Net		102,831		438,040	540,871

As of September 30, 2008, the aggregate amount of gross undeveloped acreage expiring in the next three years and thereafter are as follows: 38,811 acres in 2009 (23,289 net acres), 23,302 acres in 2010 (11,754 net acres), 82,165 acres in 2011 (67,472 net acres), and 456,734 acres thereafter (438,356 net acres).

Table of Contents**Drilling Activity**

For the Year Ended September 30	2008	Productive 2007	2006	2008	Dry 2007	2006
United States						
Gulf Coast Region						
Net Wells Completed						
Exploratory	1.14	1.31	2.94	0.37	1.42	0.85
Development		1.00	0.78		0.67	
West Coast Region						
Net Wells Completed						
Exploratory	1.00	0.50				
Development	62.00	58.99	92.98	1.00	2.00	1.00
Appalachian Region						
Net Wells Completed						
Exploratory	8.00	8.10	3.88	1.00		
Development	186.00	184.00	140.58		2.00	1.75
Total United States						
Net Wells Completed						
Exploratory	10.14	9.91	6.82	1.37	1.42	0.85
Development	248.00	243.99	234.34	1.00	4.67	2.75
Canada Discontinued Operations						
Net Wells Completed						
Exploratory		6.38	12.60			1.35
Development		1.80	2.50			1.00
Total						
Net Wells Completed						
Exploratory	10.14	16.29	19.42	1.37	1.42	2.20
Development	248.00	245.79	236.84	1.00	4.67	3.75

Present Activities

At September 30, 2008	Gulf Coast Region	West Coast Region	Appalachian Region	Total Company
Wells in Process of Drilling(1)				
Gross		2.00	1.00	148.00
Net		0.59	1.00	146.00

(1) Includes wells awaiting completion.

Item 3 Legal Proceedings

For a discussion of various environmental and other matters, refer to Part II, Item 7, MD&A and Item 8 at Note H Commitments and Contingencies. In addition to these matters, the Company is involved in other litigation and regulatory matters arising in the normal course of business. These other matters may include, for example, negligence claims and tax, regulatory or other governmental audits, inspections, investigations or other proceedings. These matters may involve state and federal taxes, safety, compliance with regulations, rate base, cost of service, and purchased gas cost issues, among other things. While these normal-course matters could have a material effect on earnings and cash flows in the quarterly and annual period in which they are

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resolved, they are not expected to change materially the Company's present liquidity position, nor are they expected to have a material adverse effect on the financial condition of the Company.

Item 4 Submission of Matters to a Vote of Security Holders

No matter was submitted to a vote of security holders during the quarter ended September 30, 2008.

PART II**Item 5 Market for the Registrant's Common Equity, Related Stockholder Matters and Issuer Purchases of Equity Securities**

Information regarding the market for the Company's common equity and related stockholder matters appears under Item 12 at Security Ownership of Certain Beneficial Owners and Management and Related Stockholder Matters, Item 8 at Note E Capitalization and Short-Term Borrowings and Note N Market for Common Stock and Related Shareholder Matters (unaudited).

On July 2, 2008, the Company issued a total of 2,400 unregistered shares of Company common stock to the eight non-employee directors of the Company then serving on the Board of Directors of the Company and receiving compensation under the Company's Retainer Policy for Non-Employee Directors, 300 shares to each such director. All of these unregistered shares were issued as partial consideration for such directors' services during the quarter ended September 30, 2008. These transactions were exempt from registration under Section 4(2) of the Securities Act of 1933, as transactions not involving a public offering.

Issuer Purchases of Equity Securities

Period	Total Number of Shares Purchased(a)	Average Price Paid per Share	Total Number of Shares Purchased as Part of Publicly Announced Share Repurchase Plans or Programs	Maximum Number of Shares that May Yet Be Purchased Under Share Repurchase Plans or Programs(b)
July 1-31, 2008	6,404	\$ 54.02		1,332,725
Aug. 1-31, 2008	544,982	\$ 46.72	537,165	795,560
Sept. 1-30, 2008	1,832,488	\$ 45.08	1,824,541	6,971,019
Total	2,383,874	\$ 45.48	2,361,706	6,971,019

(a) Represents (i) shares of common stock of the Company purchased on the open market with Company matching contributions for the accounts of participants in the Company's 401(k) plans, (ii) shares of common stock of the

Company tendered to the Company by holders of stock options or shares of restricted stock for the payment of option exercise prices or applicable withholding taxes, and (iii) shares of common stock of the Company purchased on the open market pursuant to the Company's publicly announced share repurchase program. Shares purchased other than through a publicly announced share repurchase program totaled 6,404 in July 2008, 7,817 in August 2008 and 7,947 in September 2008 (a three-month total of 22,168). All of those shares were purchased for the Company's 401(k) plans.

- (b) In December 2005, the Company's Board of Directors authorized the repurchase of up to eight million shares of the Company's common stock. The Company completed the repurchase of the eight million shares during 2008. In September 2008, the Company's Board of Directors authorized the repurchase of an additional eight million shares of the Company's common stock. The Company had, however, stopped repurchasing shares after September 17, 2008 in light of the unsettled nature of the credit markets. However, such repurchases may be made in the future if conditions improve. Such repurchases would be made in the open market or through private transactions.

Table of Contents**Item 6 Selected Financial Data**

	Year Ended September 30				
	2008	2007	2006 (Thousands)	2005	2004
Summary of Operations					
Operating Revenues	\$ 2,400,361	\$ 2,039,566	\$ 2,239,675	\$ 1,860,774	\$ 1,867,875
Operating Expenses:					
Purchased Gas	1,235,157	1,018,081	1,267,562	959,827	949,452
Operation and Maintenance	432,871	396,408	395,289	388,094	374,010
Property, Franchise and Other					
Taxes	75,585	70,660	69,202	68,164	68,378
Depreciation, Depletion and					
Amortization	170,623	157,919	151,999	156,502	159,184
	1,914,236	1,643,068	1,884,052	1,572,587	1,551,024
Loss on Sale of Timber Properties					(1,252)
Operating Income	486,125	396,498	355,623	288,187	315,599
Other Income (Expense):					
Income from Unconsolidated					
Subsidiaries	6,303	4,979	3,583	3,362	805
Impairment of Investment in					
Partnership				(4,158)	
Interest Income	10,815	1,550	9,409	6,236	1,771
Other Income	7,376	4,936	2,825	12,744	2,908
Interest Expense on Long-Term					
Debt	(70,099)	(68,446)	(72,629)	(73,244)	(82,989)
Other Interest Expense	(3,870)	(6,029)	(5,952)	(9,069)	(6,354)
Income from Continuing					
Operations Before Income Taxes	436,650	333,488	292,859	224,058	231,740
Income Tax Expense	167,922	131,813	108,245	85,621	89,820
Income from Continuing					
Operations	268,728	201,675	184,614	138,437	141,920
Discontinued Operations:					
Income (Loss) from Operations,					
Net of Tax		15,479	(46,523)	25,277	24,666
Gain on Disposal, Net of Tax		120,301		25,774	
Income (Loss) from Discontinued					
Operations, Net of Tax		135,780	(46,523)	51,051	24,666

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Net Income Available for Common Stock	\$ 268,728	\$ 337,455	\$ 138,091	\$ 189,488	\$ 166,586
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	Year Ended September 30				
	2008	2007	2006	2005	2004
	(Thousands)				
Per Common Share Data					
Basic Earnings from Continuing Operations per Common Share	\$ 3.27	\$ 2.43	\$ 2.20	\$ 1.66	\$ 1.73
Diluted Earnings from Continuing Operations per Common Share	\$ 3.18	\$ 2.37	\$ 2.15	\$ 1.63	\$ 1.71
Basic Earnings per Common Share(1)	\$ 3.27	\$ 4.06	\$ 1.64	\$ 2.27	\$ 2.03
Diluted Earnings per Common Share(1)	\$ 3.18	\$ 3.96	\$ 1.61	\$ 2.23	\$ 2.01
Dividends Declared	\$ 1.27	\$ 1.22	\$ 1.18	\$ 1.14	\$ 1.10
Dividends Paid	\$ 1.26	\$ 1.21	\$ 1.17	\$ 1.13	\$ 1.09
Dividend Rate at Year-End At September 30:	\$ 1.30	\$ 1.24	\$ 1.20	\$ 1.16	\$ 1.12
Number of Registered Shareholders	16,544	16,989	17,767	18,369	19,063
Net Property, Plant and Equipment					
Utility	\$ 1,125,859	\$ 1,099,280	\$ 1,084,080	\$ 1,064,588	\$ 1,048,428
Pipeline and Storage	826,528	681,940	674,175	680,574	696,487
Exploration and Production(2)	1,095,960	982,698	1,002,265	974,806	923,730
Energy Marketing	98	102	59	97	80
Timber	86,392	89,902	90,939	94,826	82,838
All Other	11,946	16,735	17,394	18,098	21,172
Corporate(3)	7,317	7,748	8,814	6,311	234,029
Total Net Plant	\$ 3,154,100	\$ 2,878,405	\$ 2,877,726	\$ 2,839,300	\$ 3,006,764
Total Assets	\$ 4,130,187	\$ 3,888,412	\$ 3,763,748	\$ 3,749,753	\$ 3,738,103
Capitalization					
Comprehensive Shareholders Equity	\$ 1,603,599	\$ 1,630,119	\$ 1,443,562	\$ 1,229,583	\$ 1,253,701
Long-Term Debt, Net of Current Portion	999,000	799,000	1,095,675	1,119,012	1,133,317
Total Capitalization	\$ 2,602,599	\$ 2,429,119	\$ 2,539,237	\$ 2,348,595	\$ 2,387,018

(1) Includes discontinued operations.

(2) Includes net plant of SECI discontinued operations as follows: \$0 for 2008 and 2007, \$88,023 for 2006, \$170,929 for 2005, and \$142,860 for 2004.

- (3) Includes net plant of the former international segment as follows: \$29 for 2008, \$38 for 2007, \$27 for 2006, \$20 for 2005, and \$227,905 for 2004.

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

OVERVIEW

The Company is a diversified energy company and reports financial results for five business segments. Refer to Item 1, Business, for a more detailed description of each of the segments. This Item 7, MD&A, provides information concerning:

1. The critical accounting estimates of the Company;
2. Changes in revenues and earnings of the Company under the heading, Results of Operations;
3. Operating, investing and financing cash flows under the heading Capital Resources and Liquidity;
4. Off-Balance Sheet Arrangements;
5. Contractual Obligations; and
6. Other Matters, including: (a) 2008 and 2009 funding for the Company's pension and other post-retirement benefits, (b) realizability of deferred tax assets, (c) disclosures and tables concerning market risk sensitive instruments, (d) rate and regulatory matters in the Company's New York, Pennsylvania and FERC regulated jurisdictions, (e) environmental matters, and (f) new accounting pronouncements.

The information in MD&A should be read in conjunction with the Company's financial statements in Item 8 of this report.

Overall, 2008 was a strong year for the Company. Income from continuing operations in 2008 benefited primarily from higher crude oil and natural gas prices in the Exploration and Production segment combined with an overall increase in natural gas production, primarily in the Appalachian region. These factors led to a \$67.1 million increase in income from continuing operations compared to the prior year. In 2007, the Company recorded \$135.8 million of income from discontinued operations, consisting of a \$120.3 million gain, net of tax, on the sale of SECI and \$15.5 million of income from SECI prior to its sale in August 2007. SECI, Seneca's wholly owned subsidiary, was engaged in the exploration for, and the development and purchase of, natural gas and oil reserves in the provinces of Alberta, Saskatchewan and British Columbia in Canada. Combining both income from continuing operations and discontinued operations, the Company's net income available for common stock decreased \$68.7 million in 2008 compared to the prior year. The Company's earnings are discussed further in the Results of Operations section that follows.

The Company spent \$414.5 million on capital expenditures during 2008, with approximately 46 percent being spent in the Exploration and Production segment and 40 percent being spent in the Pipeline and Storage segment. Management continues to believe that these segments provide the best earnings growth opportunities for shareholders. In the Exploration and Production segment, the Company's principal focus continues to be the development of its nearly one million acres in the Appalachian region along with continued exploration and development in the Gulf and West Coast regions. In the Pipeline and Storage segment, the majority of the expenditures were for construction costs of the Empire Connector project. The Empire Connector is anticipated to be ready to commence service in December 2008 on or before the in-service date of the Millennium Pipeline. The Company's capital expenditure program is discussed further in the Capital Resources and Liquidity section that follows.

Despite the positives mentioned above, the economy of the United States has become constrained by significant volatility and turmoil in the capital and credit markets. The government's Troubled Asset Relief Program and decreases in federal funds rates have not been enough to stem the reluctance on the part of lenders to extend credit to businesses. In the current period these events have not had a material impact on the Company, although further disruption in the markets and tightening of credit availability could negatively impact future periods. At September 30, 2008, the Company had a strong balance sheet and liquidity. The Company had no outstanding short-term notes payable to banks or commercial paper at that date. However, since that date, the Company has borrowed short-term funds under its credit lines and through the commercial paper market to fund working capital needs. The Company maintains a number of individual uncommitted or

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discretionary lines of credit with certain financial institutions for general corporate purposes. These credit lines, which aggregate to \$420.0 million, are revocable at the option of the financial institutions and are reviewed on an annual basis. The Company anticipates that these lines of credit will continue to be renewed, or replaced by similar lines. The total amount available to be issued under the Company's commercial paper program is \$300.0 million. The commercial paper program is backed by a syndicated committed credit facility totaling \$300.0 million that extends through September 30, 2010.

During 2006, the Company began repurchasing outstanding shares of common stock under a share repurchase program authorized by the Company's Board of Directors. The program authorized the Company to repurchase up to an aggregate amount of eight million shares. This threshold was reached during 2008 for a total program cost of \$324.2 million (of which 4,165,122 shares were repurchased during the year ended September 30, 2008 for \$191.0 million). In September 2008, the Company's Board of Directors authorized the repurchase of an additional eight million shares. Under this new authorization, the Company repurchased 1,028,981 shares for \$46.0 million through September 17, 2008. The Company stopped repurchasing shares after September 17, 2008 in light of the unsettled nature of the credit markets. However, such repurchases may be made in the future if conditions improve.

During 2009, the Company expects to finance its capital expenditure program, dividends, and operating expenses (including Retirement Plan and other post-retirement benefit funding) with cash from operations, proceeds from the sale of assets, and/or short-term borrowings. As oil and gas commodity prices have decreased significantly from their highs during 2008, it is possible that the Company may have to rely more heavily on short-term borrowings to meet its cash needs. It is also possible that the Company may choose to reduce its 2009 capital expenditures.

With the turmoil in the credit markets has come a significant decline in the stock markets. This has had a significant impact on the asset values of the Company's Retirement Plan and its VEBA trusts and 401(h) accounts. The Company anticipates funding \$15.0 million to \$20.0 million to the Retirement Plan and \$25.0 million to \$30.0 million to its VEBA trusts and 401(h) accounts during 2009. However, under the current funding requirements of the Pension Protection Act, should market conditions at September 30, 2008 remain unchanged, contributions in future years could increase significantly. This issue is discussed further in the Other Matters section that follows.

CRITICAL ACCOUNTING ESTIMATES

The Company has prepared its consolidated financial statements in conformity with GAAP. The preparation of these financial statements requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates. In the event estimates or assumptions prove to be different from actual results, adjustments are made in subsequent periods to reflect more current information. The following is a summary of the Company's most critical accounting estimates, which are defined as those estimates whereby judgments or uncertainties could affect the application of accounting policies and materially different amounts could be reported under different conditions or using different assumptions. For a complete discussion of the Company's significant accounting policies, refer to Item 8 at Note A - Summary of Significant Accounting Policies.

Oil and Gas Exploration and Development Costs. In the Company's Exploration and Production segment, oil and gas property acquisition, exploration and development costs are capitalized under the full cost method of accounting. Under this accounting methodology, all costs associated with property acquisition, exploration and development activities are capitalized, including internal costs directly identified with acquisition, exploration and development activities. The internal costs that are capitalized do not include any costs related to production, general corporate overhead, or similar activities. The Company does not recognize any gain or loss on the sale or other disposition of oil and gas properties unless the gain or loss would significantly alter the relationship between capitalized costs and

proved reserves of oil and gas attributable to a cost center.

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The Company believes that determining the amount of the Company's proved reserves is a critical accounting estimate. Proved reserves are estimated quantities of reserves that, based on geologic and engineering data, appear with reasonable certainty to be producible under existing economic and operating conditions. Such estimates of proved reserves are inherently imprecise and may be subject to substantial revisions as a result of numerous factors including, but not limited to, additional development activity, evolving production history and continual reassessment of the viability of production under varying economic conditions. The estimates involved in determining proved reserves are critical accounting estimates because they serve as the basis over which capitalized costs are depleted under the full cost method of accounting (on a units-of-production basis). Unproved properties are excluded from the depletion calculation until proved reserves are found or it is determined that the unproved properties are impaired. All costs related to unproved properties are reviewed quarterly to determine if impairment has occurred. The amount of any impairment is transferred to the pool of capitalized costs being amortized.

In addition to depletion under the units-of-production method, proved reserves are a major component in the SEC full cost ceiling test. The full cost ceiling test is an impairment test prescribed by SEC Regulation S-X Rule 4-10. The ceiling test, which is performed each quarter, determines a limit, or ceiling, on the amount of property acquisition, exploration and development costs that can be capitalized. The ceiling under this test represents (a) the present value of estimated future net cash flows, excluding future cash outflows associated with settling asset retirement obligations that have been accrued on the balance sheet, using a discount factor of 10%, which is computed by applying current market prices of oil and gas (as adjusted for hedging) to estimated future production of proved oil and gas reserves as of the date of the latest balance sheet, less estimated future expenditures, plus (b) the cost of unevaluated properties not being depleted, less (c) income tax effects related to the differences between the book and tax basis of the properties. The estimates of future production and future expenditures are based on internal budgets that reflect planned production from current wells and expenditures necessary to sustain such future production. The amount of the ceiling can fluctuate significantly from period to period because of additions to or subtractions from proved reserves and significant fluctuations in oil and gas prices. The ceiling is then compared to the capitalized cost of oil and gas properties less accumulated depletion and related deferred income taxes. If the capitalized costs of oil and gas properties less accumulated depletion and related deferred taxes exceeds the ceiling at the end of any fiscal quarter, a non-cash impairment must be recorded to write down the book value of the reserves to their present value. This non-cash impairment cannot be reversed at a later date if the ceiling increases. It should also be noted that a non-cash impairment to write down the book value of the reserves to their present value in any given period causes a reduction in future depletion expense. Because of the decline in the price of natural gas during the third and fourth quarters of 2006, the book value of the Company's Canadian oil and gas properties exceeded the ceiling at both June 30, 2006 and September 30, 2006. Consequently, SECI recorded impairment charges of \$62.4 million (\$39.5 million after-tax) in the third quarter of 2006 and \$42.3 million (\$29.1 million after-tax) in the fourth quarter of 2006. These impairment charges are included in the loss from discontinued operations for 2006 due to the sale of SECI during 2007. At September 30, 2008, the ceiling exceeded the book value of the Company's oil and gas properties by approximately \$500 million. Declines in commodity prices since that date have reduced the ceiling. Using more up to date pricing of \$6 per Mcf for natural gas and \$60 per barrel for crude oil, the ceiling at September 30, 2008 would have exceeded the book value of the Company's oil and gas properties by approximately \$80 million.

It is difficult to predict what factors could lead to future impairments under the SEC's full cost ceiling test. As discussed above, fluctuations in or subtractions from proved reserves and significant fluctuations in oil and gas prices have an impact on the amount of the ceiling at any point in time.

Upon the adoption of SFAS 143 on October 1, 2002, the Company recorded an asset retirement obligation representing plugging and abandonment costs associated with the Exploration and Production segment's crude oil and natural gas wells and capitalized such costs in property, plant and equipment (i.e. the full cost pool). Prior to the adoption of SFAS 143, plugging and abandonment costs were accounted for solely through the Company's units-of-production depletion calculation. An estimate of such costs was added to the depletion base, which also

included capitalized costs in the full cost pool and estimated future expenditures to be incurred in developing proved reserves. With the adoption of SFAS 143, plugging and abandonment costs are already

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included in capitalized costs and the units-of-production depletion calculation has been modified to exclude from the depletion base any estimate of future plugging and abandonment costs that are already recorded in the full cost pool.

Prior to the adoption of SFAS 143, in calculating the full cost ceiling, the Company reduced the future net cash flows from proved oil and gas reserves by the estimated plugging and abandonment costs. Such future net cash flows would then be compared to capitalized costs in the full cost pool, with any excess capitalized costs being expensed. With the adoption of SFAS 143, since the full cost pool now includes an amount associated with plugging and abandoning the wells, the calculation of the full cost ceiling has been changed so that future net cash flows from proved oil and gas reserves are no longer reduced by the estimated plugging and abandonment costs.

Regulation. The Company is subject to regulation by certain state and federal authorities. The Company, in its Utility and Pipeline and Storage segments, has accounting policies which conform to SFAS 71, and which are in accordance with the accounting requirements and ratemaking practices of the regulatory authorities. The application of these accounting policies allows the Company to defer expenses and income on the balance sheet as regulatory assets and liabilities when it is probable that those expenses and income will be allowed in the ratesetting process in a period different from the period in which they would have been reflected in the income statement by an unregulated company. These deferred regulatory assets and liabilities are then flowed through the income statement in the period in which the same amounts are reflected in rates. Management's assessment of the probability of recovery or pass through of regulatory assets and liabilities requires judgment and interpretation of laws and regulatory commission orders. If, for any reason, the Company ceases to meet the criteria for application of regulatory accounting treatment for all or part of its operations, the regulatory assets and liabilities related to those portions ceasing to meet such criteria would be eliminated from the balance sheet and included in the income statement for the period in which the discontinuance of regulatory accounting treatment occurs. Such amounts would be classified as an extraordinary item. For further discussion of the Company's regulatory assets and liabilities, refer to Item 8 at Note C Regulatory Matters.

Accounting for Derivative Financial Instruments. The Company, in its Exploration and Production segment, Energy Marketing segment, Pipeline and Storage segment and All Other category, uses a variety of derivative financial instruments to manage a portion of the market risk associated with fluctuations in the price of natural gas and crude oil. These instruments are categorized as price swap agreements, no cost collars and futures contracts. The Company, in its Pipeline and Storage segment, previously used an interest rate collar to limit interest rate fluctuations on certain variable rate debt. In accordance with the provisions of SFAS 133, the Company accounted for these instruments as effective cash flow hedges or fair value hedges. In 2007, the Company discontinued hedge accounting for the interest rate collar, which resulted in a gain being recognized. Gains or losses associated with the derivative financial instruments are matched with gains or losses resulting from the underlying physical transaction that is being hedged. To the extent that the derivative financial instruments would ever be deemed to be ineffective based on the effectiveness testing, mark-to-market gains or losses from the derivative financial instruments would be recognized in the income statement without regard to an underlying physical transaction.

The Company uses both exchange-traded and non exchange-traded derivative financial instruments. The fair values of the non exchange-traded derivative financial instruments are based on valuations determined by the counterparties. The Company used a model to substantiate the values reported by the counterparties. At September 30, 2008, the Company established a credit reserve of \$0.6 million against the asset recorded on its books for non-exchange traded derivative financial instruments. The credit reserve was determined by applying default probabilities to the anticipated cash flows that the Company is expecting from its counterparties. Refer to the Market Risk Sensitive Instruments section below for further discussion of the Company's derivative financial instruments.

Pension and Other Post-Retirement Benefits. The amounts reported in the Company's financial statements related to its pension and other post-retirement benefits are determined on an actuarial basis, which uses many assumptions in the calculation of such amounts. These assumptions include the discount rate, the expected return on plan assets, the

rate of compensation increase and, for other post-retirement benefits, the expected

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annual rate of increase in per capita cost of covered medical and prescription benefits. The Company utilizes a yield curve model to determine the discount rate. The yield curve is a spot rate yield curve that provides a zero-coupon interest rate for each year into the future. Each year's anticipated benefit payments are discounted at the associated spot interest rate back to the measurement date. The discount rate is then determined based on the spot interest rate that results in the same present value when applied to the same anticipated benefit payments. The expected return on plan assets assumption used by the Company reflects the anticipated long-term rate of return on the plan's current and future assets. The Company utilizes historical investment data, projected capital market conditions, and the plan's target asset class and investment manager allocations to set the assumption regarding the expected return on plan assets. Changes in actuarial assumptions and actuarial experience, including deviations between actual versus expected return on plan assets, could have a material impact on the amount of pension and post-retirement benefit costs and funding requirements experienced by the Company. However, the Company expects to recover substantially all of its net periodic pension and other post-retirement benefit costs attributable to employees in its Utility and Pipeline and Storage segments in accordance with the applicable regulatory commission authorization. For financial reporting purposes, the difference between the amounts of pension cost and post-retirement benefit cost recoverable in rates and the amounts of such costs as determined under applicable accounting principles is recorded as either a regulatory asset or liability, as appropriate, as discussed above under Regulation. Pension and post-retirement benefit costs for the Utility and Pipeline and Storage segments represented 97% and 93%, respectively, of the Company's total pension and post-retirement benefit costs as determined under SFAS 87 and SFAS 106 for the years ended September 30, 2008 and 2007.

Changes in actuarial assumptions and actuarial experience could also have an impact on the benefit obligation and the funded status related to the Company's pension and other post-retirement benefits and could impact the Company's equity. For example, the discount rate was changed from 6.25% in 2007 to 6.75% in 2008. The change in the discount rate from 2007 to 2008 reduced the Retirement Plan projected benefit obligation by \$38.6 million and the accumulated post-retirement benefit obligation by \$26.3 million. Other examples include actual versus expected return on plan assets, which has an impact on the funded status of the plans, and actual versus expected benefit payments, which has an impact on the pension plan projected benefit obligation and the accumulated post-retirement benefit obligation. For 2008, actual versus expected return on plan assets resulted in a decrease to the funded status of the Retirement Plan (\$94.2 million) and the VEBA trusts and 401(h) accounts (\$77.2 million). The actual versus expected benefit payments for 2008 caused an increase of \$0.1 million to the projected benefit obligation and a decrease of \$3.6 million to the accumulated post-retirement benefit obligation, respectively. In calculating the projected benefit obligation for the Retirement Plan and the accumulated post-retirement obligation, the actuary takes into account the average remaining service life of active participants. The average remaining service life of active participants is 11 years for the Retirement Plan and 13 years for those eligible for other post-retirement benefits. For further discussion of the Company's pension and other post-retirement benefits, refer to Other Matters in this Item 7, which includes a discussion of funding for the current year and the adoption of SFAS 158, and to Item 8 at Note G Retirement Plan and Other Post Retirement Benefits.

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RESULTS OF OPERATIONS

EARNINGS

2008 Compared with 2007

The Company's earnings were \$268.7 million in 2008 compared with earnings of \$337.5 million in 2007. As previously discussed, the Company presented its Canadian operations in the Exploration and Production segment (in conjunction with the sale of SECI) as discontinued operations. The Company's earnings from continuing operations were \$268.7 million in 2008 compared with \$201.7 million in 2007. The Company's earnings from discontinued operations were \$135.8 million in 2007. The increase in earnings from continuing operations is primarily the result of higher earnings in the Exploration and Production and Utility segments and the All Other category, slightly offset by lower earnings in the Corporate category and the Timber, Pipeline and Storage, and Energy Marketing segments, as shown in the table below. In the discussion that follows, note that all amounts used in the earnings discussions are after-tax amounts, unless otherwise noted. Earnings from continuing operations and discontinued operations were impacted by several events in 2008 and 2007, including:

2008 Events

A \$0.6 million gain in the All Other category associated with the sale of Horizon Power's gas-powered turbine;

2007 Events

A \$120.3 million gain on the sale of SECI, which was completed in August 2007. This amount is included in earnings from discontinued operations;

A \$4.8 million benefit to earnings in the Pipeline and Storage segment due to the reversal of a reserve established for all costs incurred related to the Empire Connector project recognized during June 2007;

A \$1.9 million benefit to earnings in the Pipeline and Storage segment associated with the discontinuance of hedge accounting for Empire's interest rate collar; and

A \$2.3 million benefit to earnings in the Energy Marketing segment related to the resolution of a purchased gas contingency.

2007 Compared with 2006

The Company's earnings were \$337.5 million in 2007 compared with earnings of \$138.1 million in 2006. As previously discussed, the Company has presented its Canadian operations in the Exploration and Production segment (in conjunction with the sale of SECI) as discontinued operations. The Company's earnings from continuing operations were \$201.7 million in 2007 compared with \$184.6 million in 2006. The Company's earnings from discontinued operations were \$135.8 million in 2007 compared with a loss of \$46.5 million in 2006. The increase in earnings from continuing operations of \$17.1 million is primarily the result of higher earnings in the Exploration and Production, Utility, Pipeline and Storage, and Energy Marketing segments and the Corporate and All Other categories, slightly offset by lower earnings in the Timber segment, as shown in the table below. The increase in earnings from discontinued operations primarily resulted from the gain on the sale of SECI recognized in 2007 as well as the non-recurrence of \$68.6 million of impairment charges recognized in 2006 related to the Exploration and Production segment's Canadian oil and gas assets. Earnings from continuing operations and discontinued operations were impacted by several events discussed above and the following 2006 events:

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\$68.6 million of impairment charges related to the Exploration and Production segment's Canadian oil and gas assets under the full cost method of accounting using natural gas pricing at June 30, 2006 and September 30, 2006;

An \$11.2 million benefit to earnings in the Exploration and Production segment (\$6.1 million in continuing operations and \$5.1 million in discontinued operations) related to income tax adjustments recognized during 2006; and

A \$2.6 million benefit to earnings in the Utility segment related to the correction of Distribution Corporation's calculation of the symmetrical sharing component of New York's gas adjustment rate.

Additional discussion of earnings in each of the business segments can be found in the business segment information that follows.

Earnings (Loss) by Segment

	Year Ended September 30		
	2008	2007	2006
	(Thousands)		
Utility	\$ 61,472	\$ 50,886	\$ 49,815
Pipeline and Storage	54,148	56,386	55,633
Exploration and Production	146,612	74,889	67,494
Energy Marketing	5,889	7,663	5,798
Timber	107	3,728	5,704
Total Reported Segments	268,228	193,552	184,444
All Other	5,672	2,564	359
Corporate	(5,172)	5,559	(189)
Total Earnings from Continuing Operations	268,728	201,675	184,614
Earnings (Loss) from Discontinued Operations		135,780	(46,523)
Total Consolidated	\$ 268,728	\$ 337,455	\$ 138,091

UTILITY**Revenues****Utility Operating Revenues**

	Year Ended September 30		
	2008	2007	2006
	(Thousands)		

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Retail Revenues:			
Residential	\$ 876,677	\$ 848,693	\$ 993,928
Commercial	135,361	136,863	166,779
Industrial	7,419	8,271	13,484
	1,019,457	993,827	1,174,191
Off-System Sales	58,225	9,751	
Transportation	113,901	102,534	92,569
Other	18,686	14,612	14,003
	\$ 1,210,269	\$ 1,120,724	\$ 1,280,763

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	Year Ended September 30		
	2008	2007	2006
Retail Sales:			
Residential	57,463	60,236	59,443
Commercial	9,769	10,713	10,681
Industrial	552	727	985
	67,784	71,676	71,109
Off-System Sales	5,686	1,355	
Transportation	64,267	62,240	57,950
	137,737	135,271	129,059

Degree Days

Year Ended September 30		Normal	Actual	Percent (Warmer) Colder Than Prior Year	
				Normal	Prior Year
2008:	Buffalo	6,729	6,277	(6.7)%	0.1%
	Erie	6,277	5,779	(7.9)%	(3.8)%
2007:	Buffalo	6,692	6,271	(6.3)%	5.1%
	Erie	6,243	6,007	(3.8)%	5.6%
2006:	Buffalo	6,692	5,968	(10.8)%	(9.4)%
	Erie	6,243	5,688	(8.9)%	(8.9)%

2008 Compared with 2007

Operating revenues for the Utility segment increased \$89.5 million in 2008 compared with 2007. This increase largely resulted from a \$48.5 million increase in off-system sales revenue (see discussion below), a \$25.6 million increase in retail gas sales revenues, an \$11.3 million increase in transportation revenues, and a \$4.1 million increase in other operating revenues.

The increase in retail gas sales revenues for the Utility segment was largely a function of the recovery of higher gas costs (subject to certain timing variations, gas costs are recovered dollar for dollar in revenues), which more than offset the revenue impact of lower retail sales volumes, as shown in the table above. See further discussion of purchased gas below under the heading Purchased Gas. This change was also affected by a base rate increase in the Pennsylvania jurisdiction (effective January 2007) that increased operating revenues by \$4.0 million for 2008. The increase is included within both retail and transportation revenues in the table above.

In the New York jurisdiction, the NYPSC issued an order providing for an annual rate increase of \$1.8 million beginning December 28, 2007. As part of this rate order, a rate design change was adopted that shifts a greater amount of cost recovery into the minimum bill amount, thus spreading the recovery of such costs more evenly throughout the year. This rate design change resulted in lower retail and transportation revenues (exclusive of the impact of higher gas costs) during the winter months compared to the prior year and higher retail and transportation revenues in the spring and summer months compared to the prior year. On a cumulative basis for 2008, the impact of this rate order has been to lower operating revenues by \$1.4 million. It is expected that there will be an increase in retail and transportation revenue in the first quarter of 2009 compared to the prior year as a result of the rate design change. The increase in transportation revenues was also due to a 2.0 Bcf increase in transportation throughput, largely the result of the migration of customers from retail sales to transportation service.

As reported in 2006, on November 17, 2006 the U.S. Court of Appeals vacated and remanded the FERC's Order No. 2004 regarding affiliate standards of conduct, with respect to natural gas pipelines. The Court's

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decision became effective on January 5, 2007, and on January 9, 2007, the FERC issued Order No. 690, its Interim Rule, designed to respond to the Court's decision. In Order No. 690, as clarified by the FERC on March 21, 2007, the FERC readopted, on an interim basis, certain provisions that existed prior to the issuance of Order No. 2004 that had made it possible for the Utility segment to engage in certain off-system sales without triggering the adverse consequences that would otherwise arise under the Order No. 2004 standards of conduct. As a result, the Utility segment resumed engaging in off-system sales on non-affiliated pipelines as of May 2007, resulting in total off-system sales revenues of \$58.2 million and \$9.8 million for 2008 and 2007, respectively. Due to profit sharing with retail customers, the margins resulting from off-system sales are minimal and there was not a material impact to margins in 2008 and 2007.

The increase in other operating revenues of \$4.1 million is largely related to amounts recorded pursuant to rate settlements approved by the NYPSC. In accordance with these settlements, Distribution Corporation was allowed to utilize certain refunds from upstream pipeline companies and certain other credits (referred to as the cost mitigation reserve) to offset certain specific expense items. In 2008, Distribution Corporation utilized \$5.6 million of the cost mitigation reserve, which increased other operating revenues, to recover previous undercollections of pension expenses. The impact of that increase in other operating revenues was offset by an equal amount of operation and maintenance expense (thus there is no earnings impact).

2007 Compared with 2006

Operating revenues for the Utility segment decreased \$160.0 million in 2007 compared with 2006. This decrease largely resulted from a \$180.4 million decrease in retail gas sales revenues. This decrease was partially offset by a \$10.0 million increase in transportation revenues and a \$9.8 million increase in off-system sales revenues.

The decrease in retail gas sales revenues for the Utility segment was largely a function of the recovery of lower gas costs (gas costs are recovered dollar for dollar in revenues), which more than offset the revenue impact of higher retail sales volumes, as shown in the table above. See further discussion of purchased gas below under the heading

Purchased Gas. This decrease was offset slightly by a base rate increase in the Pennsylvania jurisdiction, effective January 2007, which increased operating revenues by \$8.5 million for 2007. The increase is included within both retail and transportation revenues in the table above.

The increase in transportation revenues was primarily due to a 4.3 Bcf increase in transportation throughput, largely due to the migration of retail sales customers to transportation service. The corresponding \$10.0 million increase in transportation revenues would have been greater if not for a \$3.9 million out-of-period adjustment recorded in the first quarter of 2006 to correct Distribution Corporation's calculation of the symmetrical sharing component of New York's gas adjustment rate.

The increase in off-system sales revenue is due to the resumption of off-system sales in May 2007 pursuant to FERC authorization, as discussed above.

Purchased Gas

The cost of purchased gas is the Company's single largest operating expense. Annual variations in purchased gas costs are attributed directly to changes in gas sales volumes, the price of gas purchased and the operation of purchased gas adjustment clauses.

Currently, Distribution Corporation has contracted for long-term firm transportation capacity with Supply Corporation and six other upstream pipeline companies, for long-term gas supplies with a combination of producers and marketers, and for storage service with Supply Corporation and three nonaffiliated companies. In addition, Distribution

Corporation satisfies a portion of its gas requirements through spot market purchases. Changes in wellhead prices have a direct impact on the cost of purchased gas. Distribution Corporation's average cost of purchased gas, including the cost of transportation and storage, was \$11.23 per Mcf in 2008, an increase of 12% from the average cost of \$10.04 per Mcf in 2007. The average cost of purchased gas in 2007 was 17% lower than the average cost of \$12.07 per Mcf in 2006. Additional discussion of the Utility segment's gas purchases appears under the heading Sources and Availability of Raw Materials in Item 1.

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Earnings

2008 Compared with 2007

The Utility segment's earnings in 2008 were \$61.5 million, an increase of \$10.6 million when compared with earnings of \$50.9 million in 2007.

In the New York jurisdiction, earnings increased by \$6.9 million. This was primarily due to a \$3.6 million overall decrease in operating expenses (mostly other post-retirement benefits and bad debt expense), higher non-cash interest income on a pension-related regulatory asset (\$2.6 million), a decrease in property, franchise, and other taxes (\$0.9 million), a decrease in depreciation expense (\$0.8 million), lower income tax expense (\$0.7 million), lower interest expense (\$0.2 million), and increased usage per account (\$0.5 million). The impact of these items more than offset lower base rates due to the rate design change described above (\$0.9 million), and routine regulatory adjustments that reduced earnings by \$1.8 million.

In the Pennsylvania jurisdiction, earnings increased by \$3.7 million. This was primarily due to a base rate increase (\$2.6 million) that became effective January 2007, an increase in normalized usage (\$1.3 million), a decrease in bad debt expense (\$1.1 million), and a decrease in property, franchise, and other taxes (\$0.3 million). Warmer weather (\$1.6 million) partially offset these increases.

The impact of weather on the Utility segment's New York rate jurisdiction is tempered by a weather normalization clause (WNC). The WNC, which covers the eight-month period from October through May, has had a stabilizing effect on earnings for the New York rate jurisdiction. In addition, in periods of colder than normal weather, the WNC benefits the Utility segment's New York customers. In 2008 and 2007, the WNC preserved earnings of approximately \$2.5 million and \$2.3 million, respectively, as the weather was warmer than normal.

2007 Compared with 2006

The Utility segment's earnings in 2007 were \$50.9 million, an increase of \$1.1 million when compared with earnings of \$49.8 million in 2006.

In the New York jurisdiction, earnings decreased by \$6.2 million. This was primarily due to lower interest income (\$4.5 million). The New York division's current rate agreement with the NYPSC allows the Company to accrue interest on a pension-related regulatory asset. The amount of interest that can be accrued is reduced as the funded status of the pension plan improves. The fair market value of the pension plan assets exceeded the accumulated benefit obligation at September 30, 2007 resulting in a significant reduction in the interest accrual on this regulatory asset. The out-of-period symmetrical sharing adjustment discussed above (\$2.6 million), higher bad debt and other operating costs (\$0.8 million), higher property taxes (\$0.6 million), and higher interest expense (\$0.5 million) also contributed to this decrease. The positive impact associated with a lower effective tax rate (\$1.9 million) and increased usage per account (\$1.9 million) partially offset the overall decrease.

In the Pennsylvania jurisdiction, earnings increased by \$7.3 million. This was primarily due to a base rate increase (\$5.5 million) that became effective January 2007, colder weather (\$2.5 million), and the positive impact associated with a lower effective tax rate (\$1.1 million). Higher intercompany and other interest expense (\$0.8 million), coupled with a decrease in normalized usage (\$0.3 million), partially offset these increases.

The impact of weather on the Utility segment's New York rate jurisdiction is tempered by a WNC. The WNC, which covers the eight-month period from October through May, has had a stabilizing effect on earnings for the New York rate jurisdiction. In addition, in periods of colder than normal weather, the WNC benefits the Utility segment's New

York customers. In 2007 and 2006, the WNC preserved earnings of approximately \$2.3 million and \$6.2 million, respectively, as the weather was warmer than normal.

Table of Contents**PIPELINE AND STORAGE****Revenues****Pipeline and Storage Operating Revenues**

	Year Ended September 30		
	2008	2007	2006
	(Thousands)		
Firm Transportation	\$ 122,321	\$ 118,771	\$ 118,551
Interruptible Transportation	4,330	4,161	4,858
	126,651	122,932	123,409
Firm Storage Service	67,020	66,966	66,718
Interruptible Storage Service	14	169	39
	67,034	67,135	66,757
Other	22,871	21,899	24,186
	\$ 216,556	\$ 211,966	\$ 214,352

Pipeline and Storage Throughput (MMcf)

	Year Ended September 30		
	2008	2007	2006
Firm Transportation	353,173	351,113	363,379
Interruptible Transportation	5,197	4,975	11,609
	358,370	356,088	374,988

2008 Compared with 2007

Operating revenues for the Pipeline and Storage segment increased \$4.6 million in 2008 as compared with 2007. The majority of the increase was the result of increased transportation revenues (\$3.7 million) due to the fact that the Pipeline & Storage segment was able to renew existing contracts at higher rates due to favorable market conditions for transportation service associated with storage. In addition, there were increased efficiency gas revenues (\$0.8 million) reported as part of other revenues in the table above. The majority of this increase was due to higher gas prices in the current year.

2007 Compared with 2006

Operating revenues for the Pipeline and Storage segment decreased \$2.4 million in 2007 as compared with 2006, which was due mostly to a decrease in other revenues (\$2.3 million). The decrease in other revenues is primarily due to a \$4.2 million decrease in efficiency gas revenues. This decrease was due to the Company's recent settlement with the FERC, which decreased efficiency gas retainage allowances. Offsetting this decrease, there was a \$1.4 million increase in other revenues attributable to the lease termination fee adjustment in 2006 (an intercompany transaction) for the Company's former headquarters, which did not recur in 2007. While Supply Corporation's transportation volumes decreased during the year, volume fluctuations generally do not have a significant impact on revenues as a result of Supply Corporation's straight-fixed variable rate design.

Earnings

2008 Compared with 2007

The Pipeline and Storage segment's earnings in 2008 were \$54.1 million, a decrease of \$2.2 million when compared with earnings of \$56.4 million in 2007. The main factors contributing to this decrease were higher operation and maintenance expenses (\$6.1 million), primarily caused by the non-recurrence in 2008 of a reversal of a reserve for preliminary survey costs related to the Empire Connector project during 2007

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(\$4.8 million). In addition, there was a \$1.9 million positive earnings impact during 2007 associated with the discontinuance of hedge accounting for Empire's interest rate collar that did not recur during 2008, and the Pipeline and Storage segment experienced higher interest costs (\$1.5 million). These earnings decreases were offset by the earnings impact associated with higher transportation revenues (\$2.4 million), an increase in the allowance for funds used during construction (\$4.2 million) and the earnings impact associated with higher efficiency gas revenues (\$0.5 million).

2007 Compared with 2006

The Pipeline and Storage segment's earnings in 2007 were \$56.4 million, an increase of \$0.8 million when compared with earnings of \$55.6 million in 2006. The main factor contributing to this increase was the reversal of a reserve for preliminary survey costs (\$4.8 million) related to the Empire Connector project. Based on the signing of a service agreement with KeySpan Gas East Corporation during the quarter ended June 30, 2007, management determined that it was probable that the project would go forward and that such preliminary survey costs were properly capitalizable in accordance with the FERC's Uniform System of Accounts and SFAS 71. In addition, there was a \$2.5 million increase in earnings associated with the decrease in depreciation expense as a result of the most recent settlement with the FERC, which reduced depreciation rates. There was also a \$1.9 million positive earnings impact associated with the discontinuance of hedge accounting for Empire's interest rate collar. On December 8, 2006, Empire repaid \$22.8 million of secured debt. The interest costs of this secured debt were hedged by the interest rate collar. Since the hedged transaction was settled and there will be no future cash flows associated with the secured debt, the unrealized gain in accumulated other comprehensive income associated with the interest rate collar was reclassified to the income statement. These earnings increases were offset by higher interest expense (\$3.2 million), the earnings impact associated with lower efficiency gas revenues (\$2.7 million), a \$1.5 million increase in operating costs (primarily post-retirement benefit costs), and the earnings decrease associated with a higher effective tax rate (\$0.9 million).

EXPLORATION AND PRODUCTION**Revenues****Exploration and Production Operating Revenues**

	Year Ended September 30		
	2008	2007	2006
	(Thousands)		
Gas (after Hedging) from Continuing Operations	\$ 202,153	\$ 143,785	\$ 126,969
Oil (after Hedging) from Continuing Operations	250,965	167,627	134,307
Gas Processing Plant from Continuing Operations	49,090	37,528	42,252
Other from Continuing Operations	(944)	1,147	3,072
Intrasegment Elimination from Continuing Operations(1)	(34,504)	(26,050)	(31,704)
Operating Revenues from Continuing Operations	\$ 466,760	\$ 324,037	\$ 274,896
Operating Revenues from Canada Discontinued Operations	\$	\$ 50,495	\$ 71,984

(1)

Represents the elimination of certain West Coast gas production revenue included in Gas (after Hedging) from Continuing Operations in the table above that is sold to the gas processing plant shown in the table above. An elimination for the same dollar amount was made to reduce the gas processing plant's Purchased Gas expense.

Table of Contents**Production Volumes**

	Year Ended September 30		
	2008	2007	2006
Gas Production (MMcf)			
Gulf Coast	11,033	10,356	9,110
West Coast	4,039	3,929	3,880
Appalachia	7,269	5,555	5,108
Total Production from Continuing Operations	22,341	19,840	18,098
Canada Discontinued Operations		6,426	7,673
Total Production	22,341	26,266	25,771
Oil Production (Mbbbl)			
Gulf Coast	505	717	685
West Coast	2,460	2,403	2,582
Appalachia	105	124	69
Total Production from Continuing Operations	3,070	3,244	3,336
Canada Discontinued Operations		206	272
Total Production	3,070	3,450	3,608

Average Prices

	Year Ended September 30		
	2008	2007	2006
Average Gas Price/Mcf			
Gulf Coast	\$ 10.03	\$ 6.58	\$ 8.01
West Coast	\$ 8.71	\$ 6.54	\$ 7.93
Appalachia	\$ 9.73	\$ 7.48	\$ 9.53
Weighted Average for Continuing Operations	\$ 9.70	\$ 6.82	\$ 8.42
Weighted Average After Hedging for Continuing Operations(1)	\$ 9.05	\$ 7.25	\$ 7.02
Canada Discontinued Operations	\$	\$ 6.09	\$ 7.14
Average Oil Price/Barrel (bbl)			
Gulf Coast	\$ 107.27	\$ 63.04	\$ 64.10
West Coast(2)	\$ 98.17	\$ 56.86	\$ 56.80
Appalachia	\$ 97.40	\$ 62.26	\$ 65.28
Weighted Average for Continuing Operations	\$ 99.64	\$ 58.43	\$ 58.47
Weighted Average After Hedging for Continuing Operations(1)	\$ 81.75	\$ 51.68	\$ 40.26
Canada Discontinued Operations	\$	\$ 50.06	\$ 51.40

- (1) Refer to further discussion of hedging activities below under Market Risk Sensitive Instruments and in Note F Financial Instruments in Item 8 of this report.
- (2) Includes low gravity oil which generally sells for a lower price.

2008 Compared with 2007

Operating revenues from continuing operations for the Exploration and Production segment increased \$142.7 million in 2008 as compared with 2007. Oil production revenue after hedging from continuing operations increased \$83.3 million due primarily to a \$30.07 per barrel increase in weighted average prices after hedging, which more than offset a decrease in oil production of 174,000 barrels. Gas production revenue

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after hedging from continuing operations increased \$58.4 million due to a \$1.80 per Mcf increase in weighted average prices after hedging and a 2,501 MMcf increase in production. The increase in gas production from continuing operations occurred primarily in the Appalachian region (1,714 MMcf), consistent with increased drilling activity in the region. The Gulf Coast region also contributed significantly to the increase in natural gas production from continuing operations (677 MMcf). Production from new fields in 2008 (primarily in the High Island area) outpaced declines in production from some existing fields, period to period. Production in this region would have been higher if not for the hurricane activity during the month of September 2008. As a result of hurricanes Edouard, Gustav and Ike, production was shut in for much of the month of September, resulting in estimated lost production of approximately 804 MMcf of natural gas and 45 Mbbl of oil. While Seneca's properties sustained only superficial damage from the hurricanes, approximately 50% of the pre-hurricane production remains shut-in due to repair work on third party pipelines and onshore processing facilities. The majority of this production is anticipated to return by December 1, 2008.

Refer to further discussion of derivative financial instruments in the Market Risk Sensitive Instruments section that follows. Refer to the tables above for production and price information.

2007 Compared with 2006

Operating revenues from continuing operations for the Exploration and Production segment increased \$49.1 million in 2007 as compared with 2006. Oil production revenue after hedging increased \$33.3 million due primarily to an \$11.42 per barrel increase in weighted average prices after hedging, which more than offset a slight decrease in oil production of 92,000 barrels. Gas production revenue after hedging increased \$16.8 million in 2007 as compared with 2006. An increase in gas production of 1,742 MMcf and an increase in weighted average prices after hedging of \$0.23 per Mcf both contributed to the increase. The increase in gas production occurred primarily in the Gulf Coast region (1,246 MMcf). During the quarter ended December 31, 2005, Seneca experienced significant production delays due largely to the impact of hurricane damage to pipeline infrastructure in the Gulf of Mexico. Seneca had substantially all of its pre-hurricane Gulf of Mexico production back on line at the beginning of fiscal 2007. Production also increased in this segment's Appalachian region (447 MMcf), primarily due to increased drilling in this region during 2007, as highlighted in Item 2 under Exploration and Production Activities.

Refer to further discussion of derivative financial instruments in the Market Risk Sensitive Instruments section that follows. Refer to the tables above for production and price information.

Earnings**2008 Compared with 2007**

The Exploration and Production segment's earnings from continuing operations for 2008 were \$146.6 million, an increase of \$71.7 million when compared with earnings from continuing operations of \$74.9 million for 2007. Higher crude oil prices, higher natural gas prices and higher natural gas production increased earnings by \$60.0 million, \$26.2 million and \$11.8 million, respectively, while lower crude oil production decreased earnings by \$5.8 million. Higher lease operating costs (\$11.9 million), higher depletion expense (\$9.1 million), higher income tax expense (\$1.1 million) and higher general and administrative and other operating expenses (\$6.2 million) also negatively impacted earnings. Lower interest expense and higher interest income of \$6.6 million and \$0.7 million, respectively, partially offset these decreases to earnings. The increase in lease operating costs resulted from the start-up of production at the High Island 24L field in October 2007, higher steaming costs in California, and an increase in costs associated with a higher number of producing properties in Appalachia. The increase in depletion expense was caused by higher production and an increase in the depletable base. The increase in general and administrative and other operating expenses resulted from an increase in staffing and associated costs for the growing Appalachia division

combined with the recognition of actual plugging costs in excess of previously accrued amounts.

Table of Contents**2007 Compared with 2006**

The Exploration and Production segment's earnings from continuing operations for 2007 were \$74.9 million, an increase of \$7.4 million when compared with earnings from continuing operations of \$67.5 million for 2006. Higher crude oil prices, higher natural gas production and higher natural gas prices increased earnings by \$24.1 million, \$7.9 million and \$3.0 million, respectively. These increases were partly offset by the non-recurrence of \$6.1 million of tax benefits recognized during 2006, as well as by higher depletion expense and higher lease operating expense of \$7.2 million and \$4.6 million, respectively. Slightly lower crude oil production and higher general and administrative expenses also decreased earnings by \$2.4 million and \$0.6 million, respectively. Earnings were also negatively impacted by higher income tax expense (\$6.3 million).

ENERGY MARKETING**Revenues****Energy Marketing Operating Revenues**

	Year Ended September 30		
	2008	2007	2006
	(Thousands)		
Natural Gas (after Hedging)	\$ 551,243	\$ 413,405	\$ 496,769
Other	(11)	207	300
	\$ 551,232	\$ 413,612	\$ 497,069

Energy Marketing Volumes

	Year Ended September 30		
	2008	2007	2006
Natural Gas (MMcf)	56,120	50,775	45,270

2008 Compared with 2007

Operating revenues for the Energy Marketing segment increased \$137.6 million in 2008 as compared with 2007. The increase is primarily due to higher gas sales revenue, as a result of an increase in the price of natural gas that was recovered through revenues, coupled with an increase in volumes. The increase in volumes is primarily attributable to an increase in volumes sold to low-margin wholesale customers, as well as an increase in the number of commercial and industrial customers served by the Energy Marketing segment. The increase in volumes also reflects certain sales transactions undertaken to offset certain basis risks that the Energy Marketing segment was exposed to under certain commodity purchase contracts. The offsetting purchase and sale transactions had the effect of increasing revenue and volumes sold with minimal impact to earnings.

2007 Compared with 2006

Operating revenues for the Energy Marketing segment decreased \$83.5 million in 2007 as compared with 2006. The decrease primarily reflects lower gas sales revenue due to a decrease in natural gas commodity prices for the period that were recovered through revenues, offset in part by an increase in volumes. The increase in volumes was due to the addition of certain large, low-margin commercial and industrial customers, an increase in sales to wholesale customers, and colder weather.

Earnings

2008 Compared with 2007

The Energy Marketing segment's earnings in 2008 were \$5.9 million, a decrease of \$1.8 million when compared with earnings of \$7.7 million in 2007. Higher operating costs of \$1.1 million (primarily due to an increase in bad debt expense) coupled with lower margins of \$1.1 million are primarily responsible for the decrease in earnings. A major factor in the margin decrease is the non-recurrence of a purchased gas expense

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adjustment recorded during the quarter ended March 31, 2007. During that quarter, the Energy Marketing segment reversed an accrual for \$2.3 million of purchased gas expense due to a resolution of a contingency. The increase in volumes noted above, the profitable sale of certain gas held as inventory, and the marketing flexibility that the Energy Marketing segment derives from its contracts for significant storage capacity partially offset the margin decrease associated with the purchased gas adjustment.

2007 Compared with 2006

The Energy Marketing segment's earnings in 2007 were \$7.7 million, an increase of \$1.9 million when compared with earnings of \$5.8 million in 2006. Higher margins of \$2.3 million are responsible for the increase in earnings. The increase in margin is mainly the result of a \$2.3 million reversal of an accrual for purchased gas expense related to the resolution of a contingency during 2007. While volumes increased, as noted above, much of this increase in volume is related to sales to low margin customers.

TIMBER**Revenues****Timber Operating Revenues**

	Year Ended September 30		
	2008	2007	2006
	(Thousands)		
Log Sales	\$ 19,989	\$ 21,927	\$ 23,077
Green Lumber Sales	4,864	5,097	7,123
Kiln-Dried Lumber Sales	22,914	27,908	32,809
Other	1,749	3,965	2,020
	\$ 49,516	\$ 58,897	\$ 65,029

Timber Board Feet

	Year Ended September 30		
	2008	2007	2006
	(Thousands)		
Log Sales	9,272	8,660	9,527
Green Lumber Sales	9,747	9,358	10,454
Kiln-Dried Lumber Sales	13,425	14,778	16,862
	32,444	32,796	36,843

2008 Compared with 2007

Operating revenues for the Timber segment decreased \$9.4 million in 2008 as compared with 2007. Unfavorable market conditions for cherry logs and lumber combined with wet weather conditions that hampered harvesting were the main factors causing the decrease. The decrease consisted of a \$5.0 million decline in kiln-dried lumber sales. The decrease in kiln-dried lumber sales was due to both a decline in the market price of kiln-dried lumber as well as a 1,353,000 board feet decline in kiln-dried lumber sales volumes (primarily kiln-dried cherry lumber sales volumes). Log sales also decreased \$1.9 million primarily due to a decline in cherry veneer log sales volumes of 328,000 board feet. Cherry veneer logs are more valuable and sell at higher prices than other species and have the largest impact on overall log sales revenue. In addition, in 2007 the Timber segment sold 3.1 million board feet of timber rights and recorded a gain of \$1.6 million in other revenues. This event did not recur in 2008.

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2007 Compared with 2006

Operating revenues for the Timber segment decreased \$6.1 million in 2007 as compared with 2006. This decrease is attributed to unfavorable weather conditions primarily during the fall of 2006 and the spring of 2007 that greatly limited the harvesting of logs. These conditions consisted of warm, wet weather that made it difficult to bring logging trucks into the forests. Weather conditions were significantly more favorable throughout fiscal 2006. These unfavorable conditions for harvesting resulted in a decline in log sales of \$1.2 million or 867,000 board feet. There was also a decline in both green lumber and kiln-dried lumber sales of \$2.0 million and \$4.9 million, respectively, primarily because there were fewer logs available for processing. Declines in market prices for the cherry and maple species also contributed to the decrease in green lumber and kiln-dried lumber sales. Additionally, the processing of a greater amount of lumber species other than cherry (due to the mix of species on the areas being harvested) contributed to the decline in kiln-dried lumber sales since lumber species other than cherry are sold at a lower price than kiln-dried cherry lumber. Offsetting the decreases discussed above, other revenues increased \$1.9 million largely due to the sale of 3.1 million board feet of timber rights (\$1.6 million).

Earnings

2008 Compared with 2007

The Timber segment earnings in 2008 were \$0.1 million, a decrease of \$3.6 million when compared with earnings of \$3.7 million in 2007. The decrease was primarily due to lower margins from lumber, log and timber rights sales (\$4.2 million) as a result of the decline in revenues noted above. This decrease was partially offset by the earnings benefit associated with a lower effective tax rate (\$0.8 million).

2007 Compared with 2006

The Timber segment earnings in 2007 were \$3.7 million, a decrease of \$2.0 million when compared with earnings of \$5.7 million in 2006. The decrease was primarily due to lower margins from lumber and log sales (\$2.5 million) as a result of the decline in revenues noted above, as well as higher general and administrative expenses of \$0.3 million. Partially offsetting this decrease was a decline in depletion expense of \$1.2 million. The decrease in depletion expense reflects the cutting of more low cost or no cost basis timber from Company owned land as well as the overall decrease in logs harvested.

ALL OTHER AND CORPORATE OPERATIONS

All Other and Corporate operations primarily includes the operations of Horizon LFG, Horizon Power, former International segment activity and corporate operations. Horizon LFG owns and operates short-distance landfill gas pipeline companies. Horizon Power's activity primarily consists of equity method investments in Seneca Energy, Model City and ESNE. Horizon Power has a 50% ownership interest in each of these entities. The income from these equity method investments is reported as Income from Unconsolidated Subsidiaries on the Consolidated Statements of Income. Seneca Energy and Model City generate and sell electricity using methane gas obtained from landfills owned by outside parties. ESNE generates electricity from an 80-megawatt, combined cycle, natural gas-fired power plant in North East, Pennsylvania.

Earnings

2008 Compared with 2007

All Other and Corporate operations had earnings of \$0.5 million in 2008, a decrease of \$7.6 million compared with earnings of \$8.1 million for 2007. The positive earnings impact of higher income from unconsolidated subsidiaries (\$0.9 million) and a gain on the sale of a turbine by Horizon Power (\$0.6 million) were more than offset by higher operating costs (\$6.1 million), higher income tax expense (\$1.7 million) and lower interest income (\$1.3 million). The increase in operating costs is primarily the result of the proxy contest with New Mountain Vantage GP, L.L.C.

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2007 Compared with 2006

All Other and Corporate operations had earnings of \$8.1 million in 2007, an increase of \$7.9 million compared with earnings of \$0.2 million for 2006. This improvement was largely due to an increase in interest income of \$4.1 million (primarily intercompany interest). In the All Other category, Horizon LFG's earnings benefited from higher margins of \$1.0 million in 2007 as compared to 2006, and Horizon Power's income from unconsolidated subsidiaries increased \$0.9 million, also contributing to the increase in earnings. The Corporate and All Other categories also had an earnings benefit associated with lower income tax expense (\$2.0 million).

INTEREST INCOME

Interest income was \$9.3 million higher in 2008 as compared to 2007. The main reason for this increase was a \$4.0 million increase in interest income on a pension-related regulatory asset in the Utility segment's New York jurisdiction. The Exploration and Production segment also contributed \$3.8 million to this increase as a result of the investment of cash proceeds from the sale of SECI in August 2007.

Interest income was \$7.9 million lower in 2007 as compared to 2006. As discussed in the Utility earnings section above, the main reason for this decrease was a \$7.4 million decrease in interest income on a pension-related regulatory asset in the Utility segment's New York jurisdiction.

OTHER INCOME

Other income was \$2.4 million higher in 2008 as compared to 2007. This increase is attributed to the increase in the allowance for funds used during construction, in the Pipeline and Storage segment, associated with the Empire Connector project of \$4.2 million. This increase was partially offset by the non-recurrence of a death benefit gain on life insurance proceeds of \$1.9 million recognized in the Corporate category in 2007.

Other income was \$2.1 million higher in 2007 as compared to 2006. The increase is attributed to a death benefit gain on life insurance proceeds of \$1.9 million recognized in the Corporate category.

INTEREST CHARGES

Although most of the variances in Interest Charges are discussed in the earnings discussion by segment above, the following is a summary on a consolidated basis:

Interest on long-term debt increased \$1.7 million in 2008 as compared to 2007. The increase in 2008 was primarily the result of a higher average amount of long-term debt outstanding. In April 2008, the Company issued \$300 million of 6.5% senior, unsecured notes due in April 2018. This increase was partially offset by the repayment of \$200 million of 6.303% medium-term notes that matured on May 27, 2008.

Interest on long-term debt decreased \$4.2 million in 2007 as compared to 2006. The decrease in 2007 was primarily the result of a lower average amount of long-term debt outstanding. In addition, the Company recognized a \$1.9 million benefit to interest expense as a result of the discontinuance of hedge accounting for Empire's interest rate collar, as discussed above under Pipeline and Storage. The underlying long-term debt associated with this interest rate collar was repaid in December 2006 and the unrealized gain recorded in accumulated other comprehensive income associated with the interest rate collar was reclassified to interest expense during the quarter ended December 31, 2006.

Other interest charges decreased \$2.2 million in 2008 compared to 2007. Other interest charges did not change significantly in 2007 as compared to 2006. The decrease in 2008 was primarily caused by a \$1.7 million increase in the allowance for borrowed funds used during construction related to the Empire Connector project.

Table of Contents**CAPITAL RESOURCES AND LIQUIDITY**

The primary sources and uses of cash during the last three years are summarized in the following condensed statement of cash flows:

Sources (Uses) of Cash

	Year Ended September 30		
	2008	2007	2006
	(Millions)		
Provided by Operating Activities	\$ 482.8	\$ 394.2	\$ 471.4
Capital Expenditures	(397.7)	(276.7)	(294.2)
Investment in Partnership		(3.3)	
Net Proceeds from Sale of Foreign Subsidiaries		232.1	
Cash Held in Escrow	58.4	(58.2)	
Net Proceeds from Sale of Oil and Gas Producing Properties	5.9	5.1	
Other Investing Activities	4.4	(0.8)	(3.2)
Reduction of Long-Term Debt	(200.0)	(119.6)	(9.8)
Net Proceeds from Issuance of Long-Term Debt	296.6		
Issuance of Common Stock	17.4	17.5	23.3
Dividends Paid on Common Stock	(103.7)	(100.6)	(98.2)
Excess Tax Benefits Associated with Stock- Based Compensation Awards	16.3	13.7	6.5
Shares Repurchased under Repurchase Plan	(237.0)	(48.1)	(85.2)
Effect of Exchange Rates on Cash		(0.1)	1.4
Net Increase (Decrease) in Cash and Temporary Cash Investments	\$ (56.6)	\$ 55.2	\$ 12.0

OPERATING CASH FLOW

Internally generated cash from operating activities consists of net income available for common stock, adjusted for non-cash expenses, non-cash income and changes in operating assets and liabilities. Non-cash items include depreciation, depletion and amortization, impairment of oil and gas producing properties, impairment of investment in partnership, deferred income taxes, income or loss from unconsolidated subsidiaries net of cash distributions and gain on sale of discontinued operations.

Cash provided by operating activities in the Utility and Pipeline and Storage segments may vary substantially from year to year because of the impact of rate cases. In the Utility segment, supplier refunds, over- or under-recovered purchased gas costs and weather may also significantly impact cash flow. The impact of weather on cash flow is tempered in the Utility segment's New York rate jurisdiction by its WNC and in the Pipeline and Storage segment by Supply Corporation's straight fixed-variable rate design.

Cash provided by operating activities in the Exploration and Production segment may vary from period to period as a result of changes in the commodity prices of natural gas and crude oil. The Company uses various derivative financial instruments, including price swap agreements and futures contracts in an attempt to manage this energy commodity price risk.

Net cash provided by operating activities totaled \$482.8 million in 2008, an increase of \$88.6 million compared with the \$394.2 million provided by operating activities in 2007. The increase is partially due to lower working capital requirements in the Utility segment. In the Exploration and Production segment, cash provided by operations increased due to higher commodity prices, partially offset by the decrease in cash provided by operations that resulted from the sale of SECI in August 2007. Offsetting these increases were higher working capital requirements in the Energy Marketing segment.

Table of Contents**INVESTING CASH FLOW****Expenditures for Long-Lived Assets**

The Company's expenditures for long-lived assets totaled \$414.5 million in 2008. The table below presents these expenditures:

	Year Ended September 30, 2008 Total Expenditures For Long-Lived Assets (Millions)
Utility	\$ 57.5
Pipeline and Storage(1)	165.5
Exploration and Production	192.2
Timber	1.4
All Other and Corporate	0.3
Eliminations(2)	(2.4)
	\$ 414.5

(1) Amount includes \$16.8 million of accrued capital expenditures related to the Empire Connector project. This amount has been excluded from the Consolidated Statement of Cash Flows at September 30, 2008 since it represents a non-cash investing activity at that date.

(2) Represents \$2.4 million of capital expenditures included in the Appalachian region of the Exploration and Production segment for the purchase of storage facilities, buildings, and base gas from Supply Corporation during the quarter ended March 31, 2008.

Utility

The majority of the Utility capital expenditures were made for replacement of mains and main extensions, as well as for the replacement of service lines.

Pipeline and Storage

The majority of the Pipeline and Storage segment's capital expenditures were related to the Empire Connector project costs, which is discussed below under Estimated Capital Expenditures, as well as for additions, improvements and replacements to this segment's transmission and gas storage systems.

Exploration and Production

The Exploration and Production segment's capital expenditures were primarily well drilling and completion expenditures and included approximately \$63.6 million for the Gulf Coast region, substantially all of which was for the off-shore program in the shallow waters of the Gulf of Mexico, \$62.8 million for the West Coast region and \$65.8 million for the Appalachian region. These amounts included approximately \$25.4 million spent to develop proved undeveloped reserves. The Appalachian region capital expenditures include \$2.4 million for the purchase of storage facilities, buildings, and base gas from Supply Corporation, as shown in the table above.

Timber

The majority of the Timber segment capital expenditures were for construction of a lumber sorter for Highland's sawmill operations that was placed into service in October 2007 as well as for purchases of equipment for Highland's sawmill and kiln operations.

Table of Contents**All Other and Corporate**

In March 2008, Horizon Power sold a gas-powered turbine that it had planned to use in the development of a co-generation plant. Horizon Power received proceeds of \$5.3 million and recorded a pre-tax gain of \$0.9 million associated with the sale.

Estimated Capital Expenditures

The Company's estimated capital expenditures for the next three years are:

	Year Ended September 30		
	2009	2010	2011
	(Millions)		
Utility	\$ 58.0	\$ 60.0	\$ 56.0
Pipeline and Storage	73.0	76.0	46.0
Exploration and Production(1)	285.0	227.0	244.0
Timber	1.0	1.0	1.0
	\$ 417.0	\$ 364.0	\$ 347.0

(1) Includes estimated expenditures for the years ended September 30, 2009, 2010 and 2011 of approximately \$48 million, \$42 million and \$18 million, respectively, to develop proved undeveloped reserves.

Estimated capital expenditures for the Utility segment in 2009 will be concentrated in the areas of main and service line improvements and replacements and, to a lesser extent, the purchase of new equipment.

Estimated capital expenditures for the Pipeline and Storage segment in 2009 will be concentrated on the completion of the Empire Connector project as discussed below, the replacement of transmission and storage lines, the reconditioning of storage wells and improvements of compressor stations.

The Company continues to explore various opportunities to expand its capabilities to transport gas to the East Coast, either through the Supply Corporation or Empire systems or in partnership with others. Construction of the Empire Connector, a pipeline designed to transport up to approximately 250 MDth of natural gas per day that will connect the Empire Pipeline with the Millennium Pipeline, began in September 2007. The Empire Connector is anticipated to be ready to commence service in December 2008, on or before the in-service date of the Millennium Pipeline. Refer to the Rate and Regulatory Matters section that follows for further discussion of this matter. The total cost to the Company of the Empire Connector project is estimated at \$187 million, after giving effect to sales tax exemptions worth approximately \$3.7 million. As of September 30, 2008, the Company had incurred approximately \$164.7 million in costs related to this project. Of this amount, \$145.0 million, \$13.7 million and \$2.0 million were incurred during the years ended September 30, 2008, 2007 and 2006, respectively. All project costs incurred as of September 30, 2008 have been capitalized as Construction Work in Progress. The Company anticipates financing the remaining cost of this project with cash from operations.

In light of the rapidly growing demand for pipeline capacity to move natural gas from new wells being drilled in Appalachia specifically in the Marcellus Shale producing area Supply Corporation recently completed an Open

Season for its Appalachian Lateral (AppLat) pipeline project. The AppLat is expected to be routed through areas in Pennsylvania where producers are actively drilling and are seeking market access for their newly discovered reserves. The AppLat will complement Supply s original West to East (W2E) project, which was designed to transport Rockies gas supply from Clarington to the Ellisburg/Leidy/Corning area and includes the Tuscarora-to-Corning facilities previously referred to as the Tuscarora Extension. The AppLat will transport gas supply from Pennsylvania s producing area to the Overbeck area of Supply Corporation s existing system, where the facilities associated with the W2E project will move the gas to eastern market points, including Leidy, and to interconnections with Millennium and Empire at Corning.

In conjunction with the W2E and AppLat transportation projects, Supply Corporation has plans to develop new storage capacity by pursuing expansion of certain of its existing storage facilities. The expansion of these

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fields, which Supply Corporation is marketing through a recently completed Open Season concurrent with its AppLat Open Season, could provide approximately 8.5 MMDth of incremental storage capacity with incremental withdrawal deliverability of up to 121 MDth of natural gas per day, with service commencing as early as 2011. Supply Corporation expects that the availability of this incremental storage capacity will complement the W2E and AppLat pipeline projects and help meet the demand for storage created by the prospective increased flow of Appalachian and Rockies gas supply into the western Pennsylvania area, although traditional gas supplies will also be able to take advantage of this incremental storage capacity.

The timeline associated with Supply Corporation's pipeline and storage projects depends on market development. The capital cost of the AppLat/W2E project is estimated to be approximately \$800 million, and is expected to be financed by a combination of debt and equity. As of September 30, 2008, \$0.2 million has been spent to study the W2E and AppLat projects, and approximately \$0.6 million has been spent to study the storage expansion project. Costs associated with these projects have been included in preliminary survey and investigation charges and have been fully reserved for at September 30, 2008. Supply Corporation has not yet filed an application with the FERC for the authority to build either pipeline project or the storage expansion.

Estimated capital expenditures in 2009 for the Exploration and Production segment include approximately \$35.0 million for the Gulf Coast region, substantially all of which is for the off-shore program in the Gulf of Mexico, \$53.6 million for the West Coast region and \$196.3 million for the Appalachian region.

Estimated capital expenditures in 2009 in the Timber segment will be concentrated on the purchase of new equipment, vehicles and improvements to facilities for this segment's lumber yard, sawmill and kiln operations.

The Company continuously evaluates capital expenditures and investments in corporations, partnerships and other business entities. The amounts are subject to modification for opportunities such as the acquisition of attractive oil and gas properties, timber or natural gas storage facilities and the expansion of natural gas transmission line capacities. While the majority of capital expenditures in the Utility segment are necessitated by the continued need for replacement and upgrading of mains and service lines, the magnitude of future capital expenditures or other investments in the Company's other business segments depends, to a large degree, upon market conditions.

FINANCING CASH FLOW

The Company did not have any outstanding short-term notes payable to banks or commercial paper at September 30, 2008. However, the Company continues to consider short-term debt (consisting of short-term notes payable to banks and commercial paper) an important source of cash for temporarily financing capital expenditures and investments in corporations and/or partnerships, gas-in-storage inventory, unrecovered purchased gas costs, margin calls on derivative financial instruments, exploration and development expenditures, repurchases of stock, and other working capital needs. Fluctuations in these items can have a significant impact on the amount and timing of short-term debt. As for bank loans, the Company maintains a number of individual uncommitted or discretionary lines of credit with certain financial institutions for general corporate purposes. Borrowings under these lines of credit are made at competitive market rates. These credit lines, which aggregate to \$420.0 million, are revocable at the option of the financial institutions and are reviewed on an annual basis. The Company anticipates that these lines of credit will continue to be renewed, or replaced by similar lines. The total amount available to be issued under the Company's commercial paper program is \$300.0 million. The commercial paper program is backed by a syndicated committed credit facility totaling \$300.0 million that extends through September 30, 2010.

Under the Company's committed credit facility, the Company has agreed that its debt to capitalization ratio will not exceed .65 at the last day of any fiscal quarter through September 30, 2010. At September 30, 2008, the Company's debt to capitalization ratio (as calculated under the facility) was .41. The constraints specified in the committed credit

facility would permit an additional \$1.88 billion in short-term and/or long-term debt to be outstanding (further limited by the indenture covenants discussed below) before the Company's debt to capitalization ratio would exceed .65. If a downgrade in any of the Company's credit ratings were to occur, access to the commercial paper markets might not be possible. However, the Company expects that it could

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borrow under its committed credit facility, uncommitted bank lines of credit or rely upon other liquidity sources, including cash provided by operations.

Under the Company's existing indenture covenants, at September 30, 2008, the Company would have been permitted to issue up to a maximum of \$1.3 billion in additional long-term unsecured indebtedness at then current market interest rates in addition to being able to issue new indebtedness to replace maturing debt. The Company's present liquidity position is believed to be adequate to satisfy known demands.

The Company's 1974 indenture, pursuant to which \$199.0 million (or 18%) of the Company's long-term debt (as of September 30, 2008) was issued, contains a cross-default provision whereby the failure by the Company to perform certain obligations under other borrowing arrangements could trigger an obligation to repay the debt outstanding under the indenture. In particular, a repayment obligation could be triggered if the Company fails (i) to pay any scheduled principal or interest on any debt under any other indenture or agreement, or (ii) to perform any other term in any other such indenture or agreement, and the effect of the failure causes, or would permit the holders of the debt to cause, the debt under such indenture or agreement to become due prior to its stated maturity, unless cured or waived.

The Company's \$300.0 million committed credit facility also contains a cross-default provision whereby the failure by the Company or its significant subsidiaries to make payments under other borrowing arrangements, or the occurrence of certain events affecting those other borrowing arrangements, could trigger an obligation to repay any amounts outstanding under the committed credit facility. In particular, a repayment obligation could be triggered if (i) the Company or any of its significant subsidiaries fail to make a payment when due of any principal or interest on any other indebtedness aggregating \$20.0 million or more, or (ii) an event occurs that causes, or would permit the holders of any other indebtedness aggregating \$20.0 million or more to cause, such indebtedness to become due prior to its stated maturity. As of September 30, 2008, the Company had no debt outstanding under the committed credit facility.

The Company's embedded cost of long-term debt was 6.5% at September 30, 2008 and 6.4% at September 30, 2007. Refer to "Interest Rate Risk" in this Item for a more detailed breakdown of the Company's embedded cost of long-term debt.

In April 2008, the Company issued \$300.0 million of 6.50% senior, unsecured notes in a private placement exempt from registration under the Securities Act of 1933. The notes have a term of 10 years, with a maturity date in April 2018. The holders of the notes may require the Company to repurchase their notes in the event of a change in control at a price equal to 101% of the principal amount. In addition, the Company is required to either offer to exchange the notes for substantially similar notes as are registered under the Securities Act of 1933 or, in certain circumstances, register the resale of the notes. The Company used \$200.0 million of the proceeds to refund \$200.0 million of 6.303% medium-term notes that subsequently matured on May 27, 2008. In November 2008 the Company filed a registration statement with the SEC in connection with the Company's plan to offer to exchange the notes for substantially similar registered notes. The Company will seek to have the SEC declare the registration statement effective as of a date coinciding with or following the date of this report.

In December 2005, the Company's Board of Directors authorized the Company to implement a share repurchase program, whereby the Company may repurchase outstanding shares of common stock, up to an aggregate amount of eight million shares in the open market or through privately negotiated transactions. The Company completed the repurchase of the eight million shares during 2008 for a total program cost of \$324.2 million (of which 4,165,122 shares were repurchased during the year ended September 30, 2008 for \$191.0 million). In September 2008, the Company's Board of Directors authorized the repurchase of an additional eight million shares. Under this new authorization, the Company repurchased 1,028,981 shares for \$46.0 million through September 17, 2008. The Company stopped repurchasing shares after September 17, 2008 in light of the unsettled nature of the credit markets. However, such repurchases may be made in the future if conditions improve. All share repurchases mentioned above

were funded with cash provided by operating activities and/or through the use of the Company's lines of credit.

The Company may issue debt or equity securities in a public offering or a private placement from time to time. The amounts and timing of the issuance and sale of debt or equity securities will depend on market conditions, indenture requirements, regulatory authorizations and the capital requirements of the Company.

Table of Contents**OFF-BALANCE SHEET ARRANGEMENTS**

The Company has entered into certain off-balance sheet financing arrangements. These financing arrangements are primarily operating and capital leases. The Company's consolidated subsidiaries have operating leases, the majority of which are with the Utility and the Pipeline and Storage segments, having a remaining lease commitment of approximately \$32.3 million. These leases have been entered into for the use of buildings, vehicles, construction tools, meters and other items and are accounted for as operating leases. The Company's unconsolidated subsidiaries, which are accounted for under the equity method, have capital leases of electric generating equipment having a remaining lease commitment of approximately \$3.0 million. The Company has guaranteed 50%, or \$1.5 million, of these capital lease commitments.

CONTRACTUAL OBLIGATIONS

The following table summarizes the Company's expected future contractual cash obligations as of September 30, 2008, and the twelve-month periods over which they occur:

	Payments by Expected Maturity Dates						Total
	2009	2010	2011	2012	2013	Thereafter	
	(Millions)						
Long-Term Debt, including interest expense(1)	\$ 167.5	\$ 65.0	\$ 252.2	\$ 191.4	\$ 282.3	\$ 565.0	\$ 1,523.4
Operating Lease Obligations	\$ 6.0	\$ 4.6	\$ 3.6	\$ 3.2	\$ 2.5	\$ 12.4	\$ 32.3
Capital Lease Obligations	\$ 0.5	\$ 0.4	\$ 0.4	\$ 0.2	\$	\$	\$ 1.5
Purchase Obligations:							
Gas Purchase Contracts(2)	\$ 745.8	\$ 122.3	\$ 14.5	\$ 10.3	\$ 10.3	\$ 83.8	\$ 987.0
Transportation and Storage Contracts	\$ 47.4	\$ 45.7	\$ 41.1	\$ 36.7	\$ 11.3	\$ 16.9	\$ 199.1
Empire Connector Project Obligations	\$ 13.5	\$	\$	\$	\$	\$	\$ 13.5
Other	\$ 12.4	\$ 10.5	\$ 4.2	\$ 4.0	\$ 3.5	\$ 12.6	\$ 47.2

(1) Refer to Note E Capitalization and Short-Term Borrowings, as well as the table under Interest Rate Risk in the Market Risk Sensitive Instruments section below, for the amounts excluding interest expense.

(2) Gas prices are variable based on the NYMEX prices adjusted for basis.

The Company has made certain other guarantees on behalf of its subsidiaries. The guarantees relate primarily to: (i) obligations under derivative financial instruments, which are included on the consolidated balance sheet in accordance with SFAS 133 (see Item 7, MD&A under the heading Critical Accounting Estimates Accounting for Derivative Financial Instruments); (ii) NFR obligations to purchase gas or to purchase gas transportation/storage services where the amounts due on those obligations each month are included on the consolidated balance sheet as a current liability; and (iii) other obligations which are reflected on the consolidated balance sheet. The Company believes that the likelihood it would be required to make payments under the guarantees is remote, and therefore has not included them in the table above.

OTHER MATTERS

In addition to the environmental and other matters discussed in this Item 7 and in Item 8 at Note H Commitments and Contingencies, the Company is involved in other litigation and regulatory matters arising in the normal course of business. These other matters may include, for example, negligence claims and tax, regulatory or other governmental audits, inspections, investigations or other proceedings. These matters may involve state and federal taxes, safety, compliance with regulations, rate base, cost of service and purchased gas cost issues, among other things. While these normal-course matters could have a material effect on earnings and cash flows in the period in which they are resolved, they are not expected to change materially the Company's present liquidity position, nor are they expected to have a material adverse effect on the financial condition of the Company.

The Company has a tax-qualified, noncontributory defined-benefit retirement plan (Retirement Plan) that covers a majority of the Company's employees. The Company has been making contributions to the Retirement Plan over the last several years and anticipates that it will continue making contributions to the Retirement Plan. During 2008, the Company contributed \$16.0 million to the Retirement Plan. The Company anticipates that the

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annual contribution to the Retirement Plan in 2009 will be in the range of \$15.0 million to \$20.0 million. As a result of the recent downturn in the stock markets and general economic conditions, it is likely that the Company will have to fund larger amounts to the Retirement Plan subsequent to 2009 in order to be in compliance with the Pension Protection Act of 2006. The Company expects that all subsidiaries having employees covered by the Retirement Plan will make contributions to the Retirement Plan. The funding of such contributions will come from amounts collected in rates in the Utility and Pipeline and Storage segments or through short-term borrowings or through cash from operations.

The Company provides health care and life insurance benefits (other post-retirement benefits) for a majority of its retired employees. The Company has established VEBA trusts and 401(h) accounts for its other post-retirement benefits. The Company has been making contributions to its VEBA trusts and 401(h) accounts over the last several years and anticipates that it will continue making contributions to the VEBA trusts and 401(h) accounts. During 2008, the Company contributed \$29.1 million to its VEBA trusts and 401(h) accounts. The Company anticipates that the annual contribution to its VEBA trusts and 401(h) accounts in 2009 will be in the range of \$25.0 million to \$30.0 million. The funding of such contributions will come from amounts collected in rates in the Utility and Pipeline and Storage segments.

MARKET RISK SENSITIVE INSTRUMENTS**Energy Commodity Price Risk**

The Company, in its Exploration and Production segment, Energy Marketing segment, Pipeline and Storage segment, and All Other category, uses various derivative financial instruments (derivatives), including price swap agreements, no cost collars and futures contracts, as part of the Company's overall energy commodity price risk management strategy. Under this strategy, the Company manages a portion of the market risk associated with fluctuations in the price of natural gas and crude oil, thereby attempting to provide more stability to operating results. The Company has operating procedures in place that are administered by experienced management to monitor compliance with the Company's risk management policies. The derivatives are not held for trading purposes. The fair value of these derivatives, as shown below, represents the amount that the Company would receive from, or pay to, the respective counterparties at September 30, 2008 to terminate the derivatives. However, the tables below and the fair value that is disclosed do not consider the physical side of the natural gas and crude oil transactions that are related to the financial instruments.

The following tables disclose natural gas and crude oil price swap information by expected maturity dates for agreements in which the Company receives a fixed price in exchange for paying a variable price as quoted in various national natural gas publications or on the NYMEX. Notional amounts (quantities) are used to calculate the contractual payments to be exchanged under the contract. The weighted average variable prices represent the weighted average settlement prices by expected maturity date as of September 30, 2008. At September 30, 2008, the Company had not entered into any natural gas or crude oil price swap agreements extending beyond 2011.

Natural Gas Price Swap Agreements

	Expected Maturity Dates			Total
	2009	2010	2011	
Notional Quantities (Equivalent Bcf)	11.8	3.3	0.0(1)	15.1
Weighted Average Fixed Rate (per Mcf)	\$ 9.35	\$ 10.89	\$ 10.55	\$ 9.69
Weighted Average Variable Rate (per Mcf)	\$ 8.10	\$ 8.74	\$ 9.30	\$ 8.24

(1) The Energy Marketing segment has natural gas swap agreements covering approximately 40,000 Mcf in 2011.

Table of Contents**Crude Oil Price Swap Agreements**

	Expected Maturity Dates			Total
	2009	2010	2011	
Notional Quantities (Equivalent bbls)	1,260,000	600,000	60,000	1,920,000
Weighted Average Fixed Rate (per bbl)	\$ 83.12	\$ 102.52	\$ 125.25	\$ 90.50
Weighted Average Variable Rate (per bbl)	\$ 103.08	\$ 104.17	\$ 105.21	\$ 103.49

At September 30, 2008, the Company would have received from its respective counterparties an aggregate of approximately \$20.3 million to terminate the natural gas price swap agreements outstanding at that date. The Energy Marketing segment also used natural gas swaps to hedge basis risk on their fixed price purchase commitments. At September 30, 2008, the Company had natural gas basis swap agreements covering 1.4 Bcf at a weighted average fixed rate of \$0.47 (per Mcf) and a weighted average variable rate of \$0.64 (per Mcf). These natural gas swap agreements are treated as fair value hedges and the Company would have had to pay \$0.2 million at September 30, 2008 to terminate the agreements. The Company would have had to pay an aggregate of approximately \$0.8 million to its counterparties to terminate the crude oil price swap agreements outstanding at September 30, 2008.

At September 30, 2007, the Company had natural gas price swap agreements covering 13.2 Bcf at a weighted average fixed rate of \$8.20 per Mcf. The Company also had crude oil price swap agreements covering 1,485,000 bbls at a weighted average fixed rate of \$57.35 per bbl.

The following table discloses the net contract volumes purchased (sold), weighted average contract prices and weighted average settlement prices by expected maturity date for futures contracts used to manage natural gas price risk. At September 30, 2008, the Company held no futures contracts with maturity dates extending beyond 2012.

Futures Contracts

	Expected Maturity Dates				Total
	2009	2010	2011	2012	
Net Contract Volumes Purchased (Sold) (Equivalent Bcf)	2.1	0.3	(1)	(1)	2.4
Weighted Average Contract Price (per Mcf)	\$ 10.02	\$ 9.59	\$ 8.05	\$ 8.68	\$ 9.99
Weighted Average Settlement Price (per Mcf)	\$ 9.41	\$ 9.85	\$ 7.49	\$ 8.27	\$ 9.43

(1) The Energy Marketing segment has purchased 7 and 6 futures contracts (1 contract = 2,500 Dth) for 2011 and 2012, respectively.

At September 30, 2008, the Company would have received \$8.7 million to terminate these futures contracts.

At September 30, 2007, the Company had futures contracts covering 2.8 Bcf (net long position) at a weighted average contract price of \$9.11 per Mcf.

The Company may be exposed to credit risk on some of the derivatives disclosed above. Credit risk relates to the risk of loss that the Company would incur as a result of nonperformance by counterparties pursuant to the terms of their contractual obligations. To mitigate such credit risk, management performs a credit check and then, on an ongoing basis, monitors counterparty credit exposure. Management has obtained guarantees from many of the parent companies of the respective counterparties to its derivatives. At September 30, 2008, the Company had eleven counterparties for its over the counter derivative financial instruments and no individual counterparty represented greater than 42% of total credit risk (measured as volumes hedged by an individual counterparty as a percentage of the Company's total over the counter volumes hedged). The Company recorded a \$0.6 million reduction to the fair market value of its derivative assets based on its assessment of counterparty credit risk. This credit reserve was determined by applying default probabilities to the anticipated cash flows that the Company is expecting from its counterparties.

Table of Contents**Interest Rate Risk**

The following table presents the principal cash repayments and related weighted average interest rates by expected maturity date for the Company's long-term fixed rate debt as well as the other long-term debt of certain of the Company's subsidiaries. The interest rates for the variable rate debt are based on those in effect at September 30, 2008:

	Principal Amounts by Expected Maturity Dates						Total
	2009	2010	2011	2012	2013	Thereafter	
	(Dollars in millions)						
Long-Term Fixed Rate Debt	\$ 100.0(1)	\$ 200.0	\$ 150.0	\$ 250.0	\$ 399.0	\$ 1,099.0	
Weighted Average Interest Rate Paid	6.0%	7.5%	6.7%	5.3%	6.7%	6.5%	
Fair Value of Long-Term Fixed Rate Debt = \$1,027.1							

(1) These notes have been classified as Current Portion of Long-Term Debt on the Company's Consolidated Balance Sheet.

RATE AND REGULATORY MATTERS**Utility Operation**

Base rate adjustments in both the New York and Pennsylvania jurisdictions do not reflect the recovery of purchased gas costs. Such costs are recovered through operation of the purchased gas adjustment clauses of the appropriate regulatory authorities.

New York Jurisdiction

On January 29, 2007, Distribution Corporation commenced a rate case by filing proposed tariff amendments and supporting testimony requesting approval to increase its annual revenues by \$52.0 million. Following standard procedure, the NYPSC suspended the proposed tariff amendments to enable its staff and intervenors to conduct a routine investigation and hold hearings. Distribution Corporation explained in the filing that its request for rate relief was necessitated by decreased revenues resulting from customer conservation efforts and increased customer uncollectibles, among other things. The rate filing also included a proposal for an efficiency and conservation initiative with a revenue decoupling mechanism designed to render the Company indifferent to throughput reductions resulting from conservation. On September 20, 2007, the NYPSC issued an order approving, with modifications, Distribution Corporation's conservation program for implementation on an accelerated basis. Associated ratemaking issues, however, were reserved for consideration in the rate.

On December 21, 2007, the NYPSC issued a rate order providing for an annual rate increase of \$1.8 million, together with a monthly bill surcharge that would collect up to \$10.8 million to recover expenses for implementation of the conservation program. The rate increase and bill surcharge became effective December 28, 2007. The rate order further provided for a return on equity of 9.1%. The rate order also adopted Distribution Corporation's proposed revenue decoupling mechanism. The revenue decoupling mechanism, like others, decouples revenues from throughput

by enabling the Company to collect from small volume customers its allowed margin on average weather normalized usage per customer. The effect of the revenue decoupling mechanism is to render the Company financially indifferent to throughput decreases resulting from conservation. The Company surcharges or credits any difference from the average weather normalized usage per customer account. The surcharge or credit is calculated to recover total margin for the most recent twelve-month period ending December 31, and applied to customer bills annually, beginning March 1st.

On April 18, 2008, Distribution Corporation filed an appeal with Supreme Court, Albany County, seeking review of the rate order. The appeal contends that portions of the rate order should be invalidated because they fail to meet the applicable legal standard for agency decisions. Among the issues challenged by the Company are the reasonableness of the NYPSC's disallowance of expense items, including health care costs, and the

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methodology used for calculating rate of return, which the appeal contends understated the Company's cost of equity. The Company cannot predict the outcome of the appeal at this time.

Pennsylvania Jurisdiction

On June 1, 2006, Distribution Corporation filed proposed tariff amendments with PaPUC to increase annual revenues by \$25.9 million to cover increases in the cost of service to be effective July 30, 2006. The rate request was filed to address increased costs associated with Distribution Corporation's ongoing construction program as well as increases in operating costs, particularly uncollectible accounts. Following standard regulatory procedure, the PaPUC issued an order on July 20, 2006 instituting a rate proceeding and suspending the proposed tariff amendments until March 2, 2007. On October 2, 2006, the parties, including Distribution Corporation, Staff of the PaPUC and intervenors, executed an agreement (Settlement) proposing to settle all issues in the rate proceeding. The Settlement included an increase in annual revenues of \$14.3 million to non-gas revenues, an agreement not to file a rate case until January 28, 2008 at the earliest and an early implementation date. The Settlement was approved by the PaPUC at its meeting on November 30, 2006, and the new rates became effective January 1, 2007.

Pipeline and Storage

Supply Corporation currently does not have a rate case on file with the FERC. The rate settlement approved by the FERC on February 9, 2007 requires Supply Corporation to make a general rate filing to be effective December 1, 2011, and bars Supply Corporation from making a general rate filing before then, with some exceptions specified in the settlement.

Empire currently does not have a rate case on file with the NYPSC. Among the issues resolved in connection with Empire's FERC application to build the Empire Connector are the rates and terms of service that will become applicable to all of Empire's business, effective upon Empire constructing and placing its new facilities into service (currently expected for December 2008). At that time, Empire will become an interstate pipeline subject to FERC regulation. The order described in the following paragraph requires Empire to make a filing at the FERC, within three years after the in-service date, justifying Empire's existing recourse rates or proposing alternative rates.

On December 21, 2006, the FERC issued an order granting a Certificate of Public Convenience and Necessity authorizing the construction and operation of the Empire Connector and various other related pipeline projects by other unaffiliated companies. The Empire Certificate contains various environmental and other conditions. Empire accepted that Certificate and received additional environmental permits from the U.S. Army Corps of Engineers and state environmental agencies. Empire also received, from all six upstate New York counties in which it will build the Empire Connector project, final approval of sales tax exemptions and temporary partial property tax abatements. In June 2007, Empire signed a firm transportation service agreement with KeySpan Gas East Corporation, under which Empire is obligated to provide transportation service that required construction of this project. Construction began in September 2007 and is anticipated to be ready to commence service in December 2008, on or before the in-service date of the Millennium Pipeline to which it will connect.

ENVIRONMENTAL MATTERS

The Company is subject to various federal, state and local laws and regulations relating to the protection of the environment. The Company has established procedures for the ongoing evaluation of its operations to identify potential environmental exposures and comply with regulatory policies and procedures. It is the Company's policy to accrue estimated environmental clean-up costs (investigation and remediation) when such amounts can reasonably be estimated and it is probable that the Company will be required to incur such costs. At September 30, 2008, the Company has estimated its remaining clean-up costs related to former manufactured gas plant sites and third party

waste disposal sites will be in the range of \$19.4 million to \$23.6 million. The minimum estimated liability of \$19.4 million has been recorded on the Consolidated Balance Sheet at September 30, 2008. The Company expects to recover its environmental clean-up costs from a combination

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of rate recovery and deferred insurance proceeds that are currently recorded as a regulatory liability on the Consolidated Balance Sheet. Other than discussed in Note H (referred to below), the Company is currently not aware of any material additional exposure to environmental liabilities. However, changes in environmental regulations or other factors could adversely impact the Company.

For further discussion refer to Item 8 at Note H Commitments and Contingencies under the heading Environmental Matters.

NEW ACCOUNTING PRONOUNCEMENTS

In September 2006, the FASB issued SFAS 157. SFAS 157 provides guidance for using fair value to measure assets and liabilities. The pronouncement serves to clarify the extent to which companies measure assets and liabilities at fair value, the information used to measure fair value, and the effect that fair-value measurements have on earnings. SFAS 157 is to be applied whenever another standard requires or allows assets or liabilities to be measured at fair value. In accordance with FASB Staff Position FAS No. 157-2, SFAS 157 is effective for financial assets and financial liabilities that are recognized or disclosed at fair value on a recurring basis as of the Company's first quarter of fiscal 2009. The same FASB Staff Position delays the effective date for nonfinancial assets and nonfinancial liabilities, except for items that are recognized or disclosed at fair value on a recurring basis, until the Company's first quarter of fiscal 2010. The Company does not expect that SFAS 157 will have a significant impact on its consolidated financial statements.

In September 2006, the FASB also issued SFAS 158, an amendment of SFAS 87, SFAS 88, SFAS 106, and SFAS 132R. SFAS 158 requires that companies recognize a net liability or asset to report the underfunded or overfunded status of their defined benefit pension and other post-retirement benefit plans on their balance sheets, as well as recognize changes in the funded status of a defined benefit post-retirement plan in the year in which the changes occur through comprehensive income. The pronouncement also specifies that a plan's assets and obligations that determine its funded status be measured as of the end of the Company's fiscal year, with limited exceptions. In accordance with SFAS 158, the Company has recognized the funded status of its benefit plans and implemented the disclosure requirements of SFAS 158 at September 30, 2007. The requirement to measure the plan assets and benefit obligations as of the Company's fiscal year-end date will be adopted by the Company by the end of fiscal 2009. Currently, the Company measures its plan assets and benefit obligations using a June 30th measurement date. At September 30, 2007, in order to recognize the funded status of its pension and post-retirement benefit plans in accordance with SFAS 158, the Company recorded additional liabilities or reduced assets by a cumulative amount of \$78.7 million (\$71.1 million net of deferred tax benefits recognized for the portion recorded as an increase to Accumulated Other Comprehensive Loss). Of the \$71.1 million recognized, \$61.9 million was recorded as an increase to Other Regulatory Assets in the Company's Utility and Pipeline and Storage segments, \$12.5 million (net of deferred tax benefits of \$7.6 million) was recorded as an increase to Accumulated Other Comprehensive Loss, and \$3.3 million was recorded as an increase to Other Regulatory Liabilities in the Company's Utility segment. The Company has recorded amounts to Other Regulatory Assets or Other Regulatory Liabilities in the Utility and Pipeline and Storage segments in accordance with the provisions of SFAS 71. The Company, in those segments, has certain regulatory commission authorizations, which allow the Company to defer as a regulatory asset or liability the difference between pension and post-retirement benefit costs as calculated in accordance with SFAS 87 and SFAS 106 and what is collected in rates. Refer to Item 8 at Note G Retirement Plan and Other Post-Retirement Benefits for further disclosures regarding the impact of SFAS 158 on the Company's consolidated financial statements.

In February 2007, the FASB issued SFAS 159. SFAS 159 permits entities to choose to measure many financial instruments at fair value that are not otherwise required to be measured at fair value under GAAP. A company that elects the fair value option for an eligible item will be required to recognize in current earnings any changes in that item's fair value in reporting periods subsequent to the date of adoption. SFAS 159 is effective as of the Company's

first quarter of fiscal 2009. The Company does not plan to elect the fair value measurement option for any of its financial instruments other than those that are already being measured at fair value.

In December 2007, the FASB issued SFAS 141R. SFAS 141R will significantly change the accounting for business combinations in a number of areas including the treatment of contingent consideration, contingencies,

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acquisition costs, in process research and development and restructuring costs. In addition, under SFAS 141R, changes in deferred tax asset valuation allowances and acquired income tax uncertainties in a business combination after the measurement period will impact income tax expense. SFAS 141R is effective as of the Company's first quarter of fiscal 2010.

In December 2007, the FASB issued SFAS 160. SFAS 160 will change the accounting and reporting for minority interests, which will be recharacterized as noncontrolling interests (NCI) and classified as a component of equity. This new consolidation method will significantly change the accounting for transactions with minority interest holders. SFAS 160 is effective as of the Company's first quarter of fiscal 2010. The Company currently does not have any NCI.

In March 2008, the FASB issued SFAS 161. SFAS 161 requires entities to provide enhanced disclosures related to an entity's derivative instruments and hedging activities in order to enable investors to better understand how derivative instruments and hedging activities impact an entity's financial reporting. The additional disclosures include how and why an entity uses derivative instruments, how derivative instruments and related hedged items are accounted for under SFAS 133 and its related interpretations, and how derivative instruments and related hedged items affect an entity's financial position, financial performance, and cash flows. SFAS 161 is effective as of the Company's second quarter of fiscal 2009. The Company is currently evaluating the impact that the adoption of SFAS 161 will have on its disclosures in the notes to the consolidated financial statements.

EFFECTS OF INFLATION

Although the rate of inflation has been relatively low over the past few years, the Company's operations remain sensitive to increases in the rate of inflation because of its capital spending and the regulated nature of a significant portion of its business.

SAFE HARBOR FOR FORWARD-LOOKING STATEMENTS

The Company is including the following cautionary statement in this Form 10-K to make applicable and take advantage of the safe harbor provisions of the Private Securities Litigation Reform Act of 1995 for any forward-looking statements made by, or on behalf of, the Company. Forward-looking statements include statements concerning plans, objectives, goals, projections, strategies, future events or performance, and underlying assumptions and other statements which are other than statements of historical facts. From time to time, the Company may publish or otherwise make available forward-looking statements of this nature. All such subsequent forward-looking statements, whether written or oral and whether made by or on behalf of the Company, are also expressly qualified by these cautionary statements. Certain statements contained in this report, including, without limitation, statements regarding future prospects, plans, objectives, goals, projections, strategies, future events or performance and underlying assumptions, capital structure, anticipated capital expenditures, completion of construction projects, projections for pension and other post-retirement benefit obligations, impacts of the adoption of new accounting rules, and possible outcomes of litigation or regulatory proceedings, as well as statements that are identified by the use of the words anticipates, estimates, expects, forecasts, intends, plans, predicts, projects, believes, seek, similar expressions, are forward-looking statements as defined in the Private Securities Litigation Reform Act of 1995 and accordingly involve risks and uncertainties which could cause actual results or outcomes to differ materially from those expressed in the forward-looking statements. The forward-looking statements contained herein are based on various assumptions, many of which are based, in turn, upon further assumptions. The Company's expectations, beliefs and projections are expressed in good faith and are believed by the Company to have a reasonable basis, including, without limitation, management's examination of historical operating trends, data contained in the Company's records and other data available from third parties, but there can be no assurance that management's expectations, beliefs or projections will result or be achieved or accomplished. In addition to

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other factors and matters discussed elsewhere herein, the following are important factors that, in the view of the Company, could cause actual results to differ materially from those discussed in the forward-looking statements:

1. Financial and economic conditions, including the availability of credit, and their effect on the Company's ability to obtain financing on acceptable terms for working capital, capital expenditures and other investments;
2. Occurrences affecting the Company's ability to obtain financing under credit lines or other credit facilities or through the issuance of commercial paper, other short-term notes or debt or equity securities, including any downgrades in the Company's credit ratings and changes in interest rates and other capital market conditions;
3. Changes in economic conditions, including global, national or regional recessions, and their effect on the demand for, and customers' ability to pay for, the Company's products and services;
4. The creditworthiness or performance of the Company's key suppliers, customers and counterparties;
5. Economic disruptions or uninsured losses resulting from terrorist activities, acts of war, major accidents, fires, hurricanes, other severe weather, pest infestation or other natural disasters;
6. Changes in actuarial assumptions, the interest rate environment and the return on plan/trust assets related to the Company's pension and other post-retirement benefits, which can affect future funding obligations and costs and plan liabilities;
7. Changes in demographic patterns and weather conditions;
8. Changes in the availability and/or price of natural gas or oil and the effect of such changes on the accounting treatment of derivative financial instruments or the valuation of the Company's natural gas and oil reserves;
9. Impairments under the SEC's full cost ceiling test for natural gas and oil reserves;
10. Uncertainty of oil and gas reserve estimates;
11. Ability to successfully identify, drill for and produce economically viable natural gas and oil reserves, including shortages, delays or unavailability of equipment and services required in drilling operations;
12. Significant changes from expectations in the Company's actual production levels for natural gas or oil;
13. Changes in the availability and/or price of derivative financial instruments;
14. Changes in the price differentials between various types of oil;
15. Inability to obtain new customers or retain existing ones;
16. Significant changes in competitive factors affecting the Company;
17. Changes in laws and regulations to which the Company is subject, including tax, environmental, safety and employment laws and regulations;
18. Governmental/regulatory actions, initiatives and proceedings, including those involving acquisitions, financings, rate cases (which address, among other things, allowed rates of return, rate design and retained natural gas),

affiliate relationships, industry structure, franchise renewal, and environmental/safety requirements;

19. Unanticipated impacts of restructuring initiatives in the natural gas and electric industries;
20. Significant changes from expectations in actual capital expenditures and operating expenses and unanticipated project delays or changes in project costs or plans;
21. The nature and projected profitability of pending and potential projects and other investments, and the ability to obtain necessary governmental approvals and permits;
22. Ability to successfully identify and finance acquisitions or other investments and ability to operate and integrate existing and any subsequently acquired business or properties;

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23. Changes in the market price of timber and the impact such changes might have on the types and quantity of timber harvested by the Company;
24. Significant changes in tax rates or policies or in rates of inflation or interest;
25. Significant changes in the Company's relationship with its employees or contractors and the potential adverse effects if labor disputes, grievances or shortages were to occur;
26. Changes in accounting principles or the application of such principles to the Company;
27. The cost and effects of legal and administrative claims against the Company or activist shareholder campaigns to effect changes at the Company;
28. Increasing health care costs and the resulting effect on health insurance premiums and on the obligation to provide other post-retirement benefits; or
29. Increasing costs of insurance, changes in coverage and the ability to obtain insurance.

The Company disclaims any obligation to update any forward-looking statements to reflect events or circumstances after the date hereof.

Item 7A *Quantitative and Qualitative Disclosures About Market Risk*

Refer to the "Market Risk Sensitive Instruments" section in Item 7, MD&A.

Item 8 *Financial Statements and Supplementary Data*

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All other schedules are omitted because they are not applicable or the required information is shown in the Consolidated Financial Statements or Notes thereto.

Supplementary Data

Supplementary data that is included in Note M Quarterly Financial Data (unaudited) and Note O Supplementary Information for Oil and Gas Producing Activities (unaudited), appears under this Item, and reference is made thereto.

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REPORT OF INDEPENDENT REGISTERED PUBLIC ACCOUNTING FIRM

To the Board of Directors and Shareholders of National Fuel Gas Company:

In our opinion, the consolidated financial statements listed in the accompanying index present fairly, in all material respects, the financial position of National Fuel Gas Company and its subsidiaries at September 30, 2008 and 2007, and the results of their operations and their cash flows for each of the three years in the period ended September 30, 2008 in conformity with accounting principles generally accepted in the United States of America. In addition, in our opinion, the financial statement schedule listed in the accompanying index presents fairly, in all material respects, the information set forth therein when read in conjunction with the related consolidated financial statements. Also in our opinion, the Company maintained, in all material respects, effective internal control over financial reporting as of September 30, 2008, based on criteria established in *Internal Control – Integrated Framework* issued by the Committee of Sponsoring Organizations of the Treadway Commission (COSO). The Company's management is responsible for these financial statements and financial statement schedule, for maintaining effective internal control over financial reporting and for its assessment of the effectiveness of internal control over financial reporting, included in Management's Report on Internal Control over Financial Reporting appearing under Item 9A. Our responsibility is to express opinions on these financial statements, on the financial statement schedule, and on the Company's internal control over financial reporting based on our integrated audits. We conducted our audits in accordance with the standards of the Public Company Accounting Oversight Board (United States). Those standards require that we plan and perform the audits to obtain reasonable assurance about whether the financial statements are free of material misstatement and whether effective internal control over financial reporting was maintained in all material respects. Our audits of the financial statements included examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements, assessing the accounting principles used and significant estimates made by management, and evaluating the overall financial statement presentation. Our audit of internal control over financial reporting included obtaining an understanding of internal control over financial reporting, assessing the risk that a material weakness exists, and testing and evaluating the design and operating effectiveness of internal control based on the assessed risk. Our audits also included performing such other procedures as we considered necessary in the circumstances. We believe that our audits provide a reasonable basis for our opinions.

A company's internal control over financial reporting is a process designed to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles. A company's internal control over financial reporting includes those policies and procedures that (i) pertain to the maintenance of records that, in reasonable detail, accurately and fairly reflect the transactions and dispositions of the assets of the company; (ii) provide reasonable assurance that transactions are recorded as necessary to permit preparation of financial statements in accordance with generally accepted accounting principles, and that receipts and expenditures of the company are being made only in accordance with authorizations of management and directors of the company; and (iii) provide reasonable assurance regarding prevention or timely detection of unauthorized acquisition, use, or disposition of the company's assets that could have a material effect on the financial statements.

Because of its inherent limitations, internal control over financial reporting may not prevent or detect misstatements. Also, projections of any evaluation of effectiveness to future periods are subject to the risk that controls may become inadequate because of changes in conditions, or that the degree of compliance with the policies or procedures may deteriorate.

PricewaterhouseCoopers LLP

Buffalo, New York
November 26, 2008

Table of Contents**NATIONAL FUEL GAS COMPANY****CONSOLIDATED STATEMENTS OF INCOME AND EARNINGS
REINVESTED IN THE BUSINESS**

	Year Ended September 30		
	2008	2007	2006
	(Thousands of dollars, except per common share amounts)		
INCOME			
Operating Revenues	\$ 2,400,361	\$ 2,039,566	\$ 2,239,675
Operating Expenses			
Purchased Gas	1,235,157	1,018,081	1,267,562
Operation and Maintenance	432,871	396,408	395,289
Property, Franchise and Other Taxes	75,585	70,660	69,202
Depreciation, Depletion and Amortization	170,623	157,919	151,999
	1,914,236	1,643,068	1,884,052
Operating Income	486,125	396,498	355,623
Other Income (Expense):			
Income from Unconsolidated Subsidiaries	6,303	4,979	3,583
Other Income	7,376	4,936	2,825
Interest Income	10,815	1,550	9,409
Interest Expense on Long-Term Debt	(70,099)	(68,446)	(72,629)
Other Interest Expense	(3,870)	(6,029)	(5,952)
Income from Continuing Operations Before Income Taxes	436,650	333,488	292,859
Income Tax Expense	167,922	131,813	108,245
Income from Continuing Operations	268,728	201,675	184,614
Discontinued Operations:			
Income (Loss) from Operations, Net of Tax		15,479	(46,523)
Gain on Disposal, Net of Tax		120,301	
Income (Loss) from Discontinued Operations, Net of Tax		135,780	(46,523)
Net Income Available for Common Stock	268,728	337,455	138,091
EARNINGS REINVESTED IN THE BUSINESS			
Balance at Beginning of Year	983,776	786,013	813,020
	1,252,504	1,123,468	951,111
Share Repurchases	(194,776)	(38,196)	(66,269)
Cumulative Effect of Adoption of FIN 48	(406)		
Dividends on Common Stock	(103,523)	(101,496)	(98,829)

Balance at End of Year	\$	953,799	\$	983,776	\$	786,013
Earnings Per Common Share:						
Basic:						
Income from Continuing Operations	\$	3.27	\$	2.43	\$	2.20
Income (Loss) from Discontinued Operations				1.63		(0.56)
Net Income Available for Common Stock	\$	3.27	\$	4.06	\$	1.64
Diluted:						
Income from Continuing Operations	\$	3.18	\$	2.37	\$	2.15
Income (Loss) from Discontinued Operations				1.59		(0.54)
Net Income Available for Common Stock	\$	3.18	\$	3.96	\$	1.61
Weighted Average Common Shares Outstanding:						
Used in Basic Calculation		82,304,335		83,141,640		84,030,118
Used in Diluted Calculation		84,474,839		85,301,361		86,028,466

See Notes to Consolidated Financial Statements

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NATIONAL FUEL GAS COMPANY
CONSOLIDATED BALANCE SHEETS

	At September 30	
	2008	2007
	(Thousands of dollars)	
ASSETS		
Property, Plant and Equipment	\$ 4,873,969	\$ 4,461,586
Less Accumulated Depreciation, Depletion and Amortization	1,719,869	1,583,181
	3,154,100	2,878,405
Current Assets		
Cash and Temporary Cash Investments	68,239	124,806
Cash Held in Escrow		61,964
Hedging Collateral Deposits	1	4,066
Receivables Net of Allowance for Uncollectible Accounts of \$33,117 and \$28,654, Respectively	185,397	172,380
Unbilled Utility Revenue	24,364	20,682
Gas Stored Underground	87,294	66,195
Materials and Supplies at average cost	31,317	35,669
Unrecovered Purchased Gas Costs	37,708	14,769
Other Current Assets	65,158	45,057
Deferred Income Taxes		8,550
	499,478	554,138
Other Assets		
Recoverable Future Taxes	82,506	83,954
Unamortized Debt Expense	13,978	12,070
Other Regulatory Assets	189,587	137,577
Deferred Charges	4,417	5,545
Other Investments	80,640	85,902
Investments in Unconsolidated Subsidiaries	16,279	18,256
Goodwill	5,476	5,476
Intangible Assets	26,174	28,836
Prepaid Pension and Other Post-Retirement Benefit Costs	21,034	61,006
Fair Value of Derivative Financial Instruments	28,786	9,188
Other	7,732	8,059
	476,609	455,869
Total Assets	\$ 4,130,187	\$ 3,888,412

CAPITALIZATION AND LIABILITIES

Capitalization:**Comprehensive Shareholders Equity**

Common Stock, \$1 Par Value

Authorized 200,000,000 Shares; Issued and Outstanding 79,120,544 Shares and 83,461,308 Shares, Respectively	\$ 79,121	\$ 83,461
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Paid In Capital	567,716	569,085
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Earnings Reinvested in the Business	953,799	983,776
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Total Common Shareholders Equity Before Items Of Other Comprehensive Income (Loss)	1,600,636	1,636,322
Accumulated Other Comprehensive Income (Loss)	2,963	(6,203)

Total Comprehensive Shareholders Equity	1,603,599	1,630,119
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Long-Term Debt, Net of Current Portion	999,000	799,000
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Total Capitalization	2,602,599	2,429,119
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Current and Accrued Liabilities

Notes Payable to Banks and Commercial Paper

Current Portion of Long-Term Debt	100,000	200,024
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Accounts Payable	142,520	109,757
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Amounts Payable to Customers	2,753	10,409
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Dividends Payable	25,714	25,873
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Interest Payable on Long-Term Debt	22,114	18,158
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Customer Advances	33,017	22,863
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Other Accruals and Current Liabilities	45,220	36,062
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Deferred Income Taxes	1,871	
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Fair Value of Derivative Financial Instruments	1,362	16,200
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	374,571	439,346
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Deferred Credits

Deferred Income Taxes	634,372	575,356
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Taxes Refundable to Customers	18,449	14,026
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Unamortized Investment Tax Credit	4,691	5,392
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Cost of Removal Regulatory Liability	103,100	91,226
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Other Regulatory Liabilities	91,933	76,659
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Pension and Other Post-Retirement Liabilities	78,909	70,555
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Asset Retirement Obligations	93,247	75,939
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Other Deferred Credits	128,316	110,794
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	1,153,017	1,019,947
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Commitments and Contingencies

Total Capitalization and Liabilities	\$ 4,130,187	\$ 3,888,412
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See Notes to Consolidated Financial Statements

Table of Contents**NATIONAL FUEL GAS COMPANY****CONSOLIDATED STATEMENTS OF CASH FLOWS**

	Year Ended September 30		
	2008	2007	2006
	(Thousands of dollars)		
Operating Activities			
Net Income Available for Common Stock	\$ 268,728	\$ 337,455	\$ 138,091
Adjustments to Reconcile Net Income to Net Cash Provided by Operating Activities:			
Gain on Sale of Discontinued Operations		(159,873)	
Impairment of Oil and Gas Producing Properties			104,739
Depreciation, Depletion and Amortization	170,623	170,803	179,615
Deferred Income Taxes	72,496	52,847	(5,230)
Income from Unconsolidated Subsidiaries, Net of Cash Distributions	1,977	(3,366)	1,067
Excess Tax Benefits Associated with Stock-Based Compensation Awards	(16,275)	(13,689)	(6,515)
Other	4,858	16,399	4,829
Change in:			
Hedging Collateral Deposits	4,065	15,610	58,108
Receivables and Unbilled Utility Revenue	(16,815)	5,669	(12,343)
Gas Stored Underground and Materials and Supplies	(22,116)	(5,714)	1,679
Unrecovered Purchased Gas Costs	(22,939)	(1,799)	1,847
Prepayments and Other Current Assets	(36,376)	18,800	(39,572)
Accounts Payable	32,763	(26,002)	(23,144)
Amounts Payable to Customers	(7,656)	(13,526)	22,777
Customer Advances	10,154	(6,554)	4,946
Other Accruals and Current Liabilities	(3,641)	8,950	(17,754)
Other Assets	(11,887)	4,109	(22,700)
Other Liabilities	54,817	(5,922)	80,960
Net Cash Provided by Operating Activities	482,776	394,197	471,400
Investing Activities			
Capital Expenditures	(397,734)	(276,728)	(294,159)
Investment in Partnership		(3,300)	
Net Proceeds from Sale of Foreign Subsidiaries		232,092	
Cash Held in Escrow	58,397	(58,248)	
Net Proceeds from Sale of Oil and Gas Producing Properties	5,969	5,137	13
Other	4,376	(725)	(3,230)
Net Cash Used in Investing Activities	(328,992)	(101,772)	(297,376)
Financing Activities			
Excess Tax Benefits Associated with Stock-Based Compensation Awards	16,275	13,689	6,515

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Shares Repurchased under Repurchase Plan	(237,006)	(48,070)	(85,168)
Net Proceeds from Issuance of Long-Term Debt	296,655		
Reduction of Long-Term Debt	(200,024)	(119,576)	(9,805)
Net Proceeds from Issuance of Common Stock	17,432	17,498	23,339
Dividends Paid on Common Stock	(103,683)	(100,632)	(98,266)
Net Cash Used in Financing Activities	(210,351)	(237,091)	(163,385)
Effect of Exchange Rates on Cash		(139)	1,365
Net Increase (Decrease) in Cash and Temporary Cash Investments	(56,567)	55,195	12,004
Cash and Temporary Cash Investments At Beginning of Year	124,806	69,611	57,607
Cash and Temporary Cash Investments At End of Year	\$ 68,239	\$ 124,806	\$ 69,611
Supplemental Disclosure of Cash Flow Information			
Cash Paid For:			
Interest	\$ 69,841	\$ 75,987	\$ 78,003
Income Taxes	\$ 103,154	\$ 97,961	\$ 54,359

See Notes to Consolidated Financial Statements

Table of Contents**NATIONAL FUEL GAS COMPANY****CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME**

	Year Ended September 30		
	2008	2007	2006
	(Thousands of dollars)		
Net Income Available for Common Stock	\$ 268,728	\$ 337,455	\$ 138,091
Other Comprehensive Income (Loss), Before Tax:			
Minimum Pension Liability Adjustment			165,914
Decrease in the Funded Status of the Pension and Other Post-Retirement Benefit Plans	(13,584)		
Reclassification Adjustment for Amortization of Prior Year Funded Status of the Pension and Other Post-Retirement Benefit Plans	1,924		
Foreign Currency Translation Adjustment	12	7,874	7,408
Reclassification Adjustment for Realized Foreign Currency Translation Gain in Net Income		(42,658)	(716)
Unrealized Gain (Loss) on Securities Available for Sale Arising During the Period	(4,856)	4,747	2,573
Unrealized Gain (Loss) on Derivative Financial Instruments Arising During the Period	(31,490)	8,495	90,196
Reclassification Adjustment for Realized Losses on Derivative Financial Instruments in Net Income	64,645	5,106	91,743
Other Comprehensive Income (Loss), Before Tax	16,651	(16,436)	357,118
Income Tax Expense Related to Minimum Pension Liability Adjustment			58,070
Income Tax Benefit Related to the Decrease in the Funded Status of the Pension and Other Post-Retirement Benefit Plans	(5,127)		
Reclassification Adjustment for Income Tax Benefit Related to the Amortization of the Prior Year Funded Status of the Pension and Other Post-Retirement Benefit Plans	726		
Income Tax Expense (Benefit) Related to Unrealized Gain (Loss) on Securities Available for Sale Arising During the Period	(1,434)	1,724	894
Income Tax Expense (Benefit) Related to Unrealized Gain (Loss) on Derivative Financial Instruments Arising During the Period	(13,228)	3,153	34,772
Reclassification Adjustment for Income Tax Benefit on Realized Losses on Derivative Financial Instruments In Net Income	26,548	2,824	35,338
Income Taxes Net	7,485	7,701	129,074
Other Comprehensive Income (Loss)	9,166	(24,137)	228,044
Comprehensive Income	\$ 277,894	\$ 313,318	\$ 366,135

See Notes to Consolidated Financial Statements

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NATIONAL FUEL GAS COMPANY

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

Note A Summary of Significant Accounting Policies

Principles of Consolidation

The Company consolidates its majority owned entities. The equity method is used to account for minority owned entities. All significant intercompany balances and transactions are eliminated. The Company uses proportionate consolidation when accounting for drilling arrangements related to oil and gas producing properties accounted for under the full cost method of accounting.

The preparation of the consolidated financial statements in conformity with GAAP requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates.

Regulation

The Company is subject to regulation by certain state and federal authorities. The Company has accounting policies which conform to GAAP, as applied to regulated enterprises, and are in accordance with the accounting requirements and ratemaking practices of the regulatory authorities. Reference is made to Note C Regulatory Matters for further discussion.

Revenue Recognition

The Company's Utility segment records revenue as bills are rendered, except that service supplied but not billed is reported as unbilled utility revenue and is included in operating revenues for the year in which service is furnished.

The Company's Energy Marketing segment records revenue as bills are rendered for service supplied on a calendar month basis.

The Company's Pipeline and Storage segment records revenue for natural gas transportation and storage services. Revenue from reservation charges on firm contracted capacity is recognized through equal monthly charges over the contract period regardless of the amount of gas that is transported or stored. Commodity charges on firm contracted capacity and interruptible contracts are recognized as revenue when physical deliveries of natural gas are made at the agreed upon delivery point or when gas is injected or withdrawn from the storage field. The point of delivery into the pipeline or injection or withdrawal from storage is the point at which ownership and risk of loss transfers to the buyer of such transportation and storage services.

The Company's Timber segment records revenue on lumber and log sales as products are shipped, which is the point at which ownership and risk of loss transfers to the buyer of lumber products or logs.

The Company's Exploration and Production segment records revenue based on entitlement, which means that revenue is recorded based on the actual amount of gas or oil that is delivered to a pipeline and the Company's ownership interest in the producing well. If a production imbalance occurs between what was supposed to be delivered to a pipeline and what was actually produced and delivered, the Company accrues the difference as an imbalance.

Allowance for Uncollectible Accounts

The allowance for uncollectible accounts is the Company's best estimate of the amount of probable credit losses in the existing accounts receivable. The allowance is determined based on historical experience, the age and other specific information about customer accounts. Account balances are charged off against the allowance twelve months after the account is final billed or when it is anticipated that the receivable will not be recovered.

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NATIONAL FUEL GAS COMPANY

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)

Regulatory Mechanisms

The Company's rate schedules in the Utility segment contain clauses that permit adjustment of revenues to reflect price changes from the cost of purchased gas included in base rates. Differences between amounts currently recoverable and actual adjustment clause revenues, as well as other price changes and pipeline and storage company refunds not yet includable in adjustment clause rates, are deferred and accounted for as either unrecovered purchased gas costs or amounts payable to customers. Such amounts are generally recovered from (or passed back to) customers during the following fiscal year.

Estimated refund liabilities to ratepayers represent management's current estimate of such refunds. Reference is made to Note C – Regulatory Matters for further discussion.

The impact of weather on revenues in the Utility segment's New York rate jurisdiction is tempered by a WNC, which covers the eight-month period from October through May. The WNC is designed to adjust the rates of retail customers to reflect the impact of deviations from normal weather. Weather that is warmer than normal results in a surcharge being added to customers' current bills, while weather that is colder than normal results in a refund being credited to customers' current bills. Since the Utility segment's Pennsylvania rate jurisdiction does not have a WNC, weather variations have a direct impact on the Pennsylvania rate jurisdiction's revenues.

In the Pipeline and Storage segment, the allowed rates that Supply Corporation bills its customers are based on a straight fixed-variable rate design, which allows recovery of all fixed costs in fixed monthly reservation charges. The allowed rates that Empire bills its customers are based on a modified fixed-variable rate design, which allows recovery of most fixed costs in fixed monthly reservation charges. To distinguish between the two rate designs, the modified fixed-variable rate design recovers return on equity and income taxes through variable charges whereas straight fixed-variable recovers all fixed costs, including return on equity and income taxes, through its monthly reservation charge. Because of the difference in rate design, changes in throughput due to weather variations do not have a significant impact on Supply Corporation's revenues but may have a significant impact on Empire's revenues.

Property, Plant and Equipment

The principal assets of the Utility and Pipeline and Storage segments, consisting primarily of gas plant in service, are recorded at the historical cost when originally devoted to service in the regulated businesses, as required by regulatory authorities.

In the Company's Exploration and Production segment, oil and gas property acquisition, exploration and development costs are capitalized under the full cost method of accounting. Under this methodology, all costs associated with property acquisition, exploration and development activities are capitalized, including internal costs directly identified with acquisition, exploration and development activities. The internal costs that are capitalized do not include any costs related to production, general corporate overhead, or similar activities. The Company does not recognize any gain or loss on the sale or other disposition of oil and gas properties unless the gain or loss would significantly alter the relationship between capitalized costs and proved reserves of oil and gas attributable to a cost center.

Capitalized costs include costs related to unproved properties, which are excluded from amortization until proved reserves are found or it is determined that the unproved properties are impaired. All costs related to unproved

properties are reviewed quarterly to determine if impairment has occurred. The amount of any impairment is transferred to the pool of capitalized costs being amortized.

Capitalized costs are subject to the SEC full cost ceiling test. The ceiling test, which is performed each quarter, determines a limit, or ceiling, on the amount of property acquisition, exploration and development costs that can be capitalized. The ceiling under this test represents (a) the present value of estimated future net

Table of Contents**NATIONAL FUEL GAS COMPANY****NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)**

cash flows, excluding future cash outflows associated with settling asset retirement obligations that have been accrued on the balance sheet, using a discount factor of 10%, which is computed by applying current market prices of oil and gas (as adjusted for hedging) to estimated future production of proved oil and gas reserves as of the date of the latest balance sheet, less estimated future expenditures, plus (b) the cost of unevaluated properties not being depleted, less (c) income tax effects related to the differences between the book and tax basis of the properties. If capitalized costs, net of accumulated depreciation, depletion and amortization and related deferred income taxes, exceed the ceiling at the end of any quarter, a permanent impairment is required to be charged to earnings in that quarter. In adjusting estimated future net cash flows for hedging under the ceiling test at September 30, 2008, 2007, and 2006, estimated future net cash flows were increased by \$34.5 million, \$2.2 million and \$4.7 million, respectively. The Company's capitalized costs exceeded the full cost ceiling for the Company's Canadian properties at June 30, 2006 and September 30, 2006. As such, the Company recognized pre-tax impairments of \$62.4 million at June 30, 2006 and \$42.3 million at September 30, 2006. These impairment charges are included in loss from discontinued operations for 2006 due to the sale of SECI during 2007.

Maintenance and repairs of property and replacements of minor items of property are charged directly to maintenance expense. The original cost of the regulated subsidiaries' property, plant and equipment retired, and the cost of removal less salvage, are charged to accumulated depreciation.

Depreciation, Depletion and Amortization

For oil and gas properties, depreciation, depletion and amortization is computed based on quantities produced in relation to proved reserves using the units of production method. The cost of unproved oil and gas properties is excluded from this computation. For timber properties, depletion, determined on a property by property basis, is charged to operations based on the actual amount of timber cut in relation to the total amount of recoverable timber. For all other property, plant and equipment, depreciation, depletion and amortization is computed using the straight-line method in amounts sufficient to recover costs over the estimated service lives of property in service. The following is a summary of depreciable plant by segment:

	As of September 30	
	2008	2007
	(Thousands)	
Utility	\$ 1,580,366	\$ 1,539,808
Pipeline and Storage	996,743	976,316
Exploration and Production	1,800,422	1,577,745
Energy Marketing	1,232	1,199
Timber	120,021	119,237
All Other and Corporate	25,984	32,806
	\$ 4,524,768	\$ 4,247,111

Average depreciation, depletion and amortization rates are as follows:

	Year Ended September 30		
	2008	2007	2006
Utility	2.6%	2.8%	2.8%
Pipeline and Storage	3.2%	3.5%	4.0%
Exploration and Production, per Mcfe(1)	\$ 2.26	\$ 1.94	\$ 2.00
Energy Marketing	3.5%	2.8%	4.8%
Timber	4.1%	4.0%	5.6%
All Other and Corporate	5.0%	4.6%	4.1%

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NATIONAL FUEL GAS COMPANY

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)

- (1) Amounts include depletion of oil and gas producing properties as well as depreciation of fixed assets. As disclosed in Note O – Supplementary Information for Oil and Gas Producing Properties, depletion of oil and gas producing properties amounted to \$2.23, \$1.92 and \$1.98 per Mcfe of production in 2008, 2007 and 2006, respectively. Depletion of oil and gas producing properties in the United States amounted to \$2.23, \$1.97 and \$1.74 per Mcfe of production in 2008, 2007 and 2006, respectively. Depletion of oil and gas producing properties in Canada amounted \$1.67 and \$2.95 per Mcfe of production in 2007 and 2006, respectively.

Goodwill

The Company has recognized goodwill of \$5.5 million as of September 30, 2008 and 2007 on its consolidated balance sheet related to the Company's acquisition of Empire in 2003. The Company accounts for goodwill in accordance with SFAS 142, which requires the Company to test goodwill for impairment annually. At September 30, 2008 and 2007, the fair value of Empire was greater than its book value. As such, the goodwill was considered not impaired.

Financial Instruments

Unrealized gains or losses from the Company's investments in an equity mutual fund and the stock of an insurance company (securities available for sale) are recorded as a component of accumulated other comprehensive income (loss). Reference is made to Note F – Financial Instruments for further discussion.