

LACLEDE GROUP INC
Form 10-Q
April 30, 2013

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

FORM 10-Q

☒ QUARTERLY REPORT PURSUANT TO SECTION 13 or 15 (d) OF THE SECURITIES EXCHANGE
ACT OF 1934 For the Quarter Ended March 31, 2013

OR

☐ TRANSITION REPORT PURSUANT TO SECTION 13 or 15 (d) OF THE SECURITIES EXCHANGE
ACT OF 1934 For the Transition Period from – _____ to _____

Commission File Number 1-16681

THE LACLEDE GROUP, INC.

(Exact name of registrant as specified in its charter)

Missouri

74-2976504

(State of Incorporation)

(I.R.S. Employer Identification number)

720 Olive Street

St. Louis, MO 63101

(Address and zip code of principal executive offices)

314-342-0500

(Registrant's telephone number, including area code)

Indicate by check mark if the registrant:

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

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

is a large accelerated filer, an accelerated filer, a non-accelerated filer, or a smaller reporting company. See the definitions of "large accelerated filer," "accelerated filer," and "smaller reporting company" in Rule 12b-2 of the Exchange Act.

Large accelerated filer ☒

Accelerated filer ☐

Non-accelerated filer ☐

Smaller reporting company ☐

is a shell company (as defined in Rule 12b-2 of the Exchange Act). Yes ☐ No ☒

As of April 26, 2013, there were 22,671,392 shares of the registrant's Common Stock, par value \$1.00 per share, outstanding.

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PART I. FINANCIAL INFORMATION

The interim financial statements included herein have been prepared by The Laclede Group, Inc. (Laclede Group or the Company), without audit, pursuant to the rules and regulations of the Securities and Exchange Commission (SEC). These financial statements should be read in conjunction with the financial statements and the notes thereto included in the Company's Form 10-K for the fiscal year ended September 30, 2012.

Item 1. Financial Statements

THE LACLEDE GROUP, INC.
 STATEMENTS OF CONSOLIDATED INCOME
 (UNAUDITED)

	Three Months Ended March 31,		Six Months Ended March 31,	
(Thousands, Except Per Share Amounts)	2013	2012	2013	2012
Operating Revenues:				
Gas Utility	\$354,097	\$298,620	\$604,208	\$549,522
Gas Marketing	41,255	59,434	96,504	218,022
Other	2,261	121	3,904	1,544
Total Operating Revenues	397,613	358,175	704,616	769,088
Operating Expenses:				
Gas Utility				
Natural and propane gas	230,440	171,164	366,956	317,915
Other operation expenses	35,267	38,043	69,187	75,608
Maintenance	5,924	5,761	11,655	11,069
Depreciation and amortization	11,258	10,175	22,223	20,264
Taxes, other than income taxes	21,751	20,093	36,557	34,760
Total Gas Utility Operating Expenses	304,640	245,236	506,578	459,616
Gas Marketing	35,995	61,805	93,376	214,364
Other	5,129	551	10,727	1,420
Total Operating Expenses	345,764	307,592	610,681	675,400
Operating Income	51,849	50,583	93,935	93,688
Other Income and (Income Deductions) – Net	1,340	1,381	2,424	3,320
Interest Charges:				
Interest on long-term debt	5,689	5,740	11,127	11,479
Other interest charges	1,016	539	1,604	1,114
Total Interest Charges	6,705	6,279	12,731	12,593
Income Before Income Taxes	46,484	45,685	83,628	84,415
Income Tax Expense	16,242	16,001	27,818	29,557
Net Income	\$30,242	\$29,684	\$55,810	\$54,858
Weighted Average Number of Common Shares Outstanding:				
Basic	22,421	22,254	22,396	22,223
Diluted	22,498	22,336	22,466	22,299
Basic Earnings Per Share of Common Stock	\$1.34	\$1.33	\$2.48	\$2.45
Diluted Earnings Per Share of Common Stock	\$1.34	\$1.32	\$2.47	\$2.45
Dividends Declared Per Share of Common Stock	\$0.425	\$0.415	\$0.850	\$0.830
See <u>Notes to Consolidated Financial Statements</u> .				

THE LACLEDE GROUP, INC.
STATEMENTS OF CONSOLIDATED COMPREHENSIVE INCOME
(UNAUDITED)

	Three Months Ended March 31,		Six Months Ended March 31,	
(Thousands)	2013	2012	2013	2012
Net Income	\$30,242	\$29,684	\$55,810	\$54,858
Other Comprehensive Income (Loss), Before Tax:				
Net gains (losses) on cash flow hedging derivative instruments:				
Net hedging (loss) gain arising during the period	(7,590	) 5,106	(6,201	) 8,153
Reclassification adjustment for (gains) losses included in net income	(22	) 408	2,228	(2,422)
Net unrealized gains (losses) on cash flow hedging derivative instruments	(7,612	) 5,514	(3,973	) 5,731
Defined benefit pension and other postretirement plans:				
Net actuarial loss arising during the period	—	(2,366	) —	(2,366)
Amortization of actuarial loss included in net periodic pension and postretirement benefit cost	90	3,482	181	3,573
Net defined benefit pension and other postretirement plans	90	1,116	181	1,207
Other Comprehensive Income (Loss), Before Tax	(7,522	) 6,630	(3,792	) 6,938
Income Tax (Benefit) Expense Related to Items of Other Comprehensive Income	(2,868	) 2,561	(1,417	) 2,680
Other Comprehensive (Loss) Income, Net of Tax	(4,654	) 4,069	(2,375	) 4,258
Comprehensive Income	\$25,588	\$33,753	\$53,435	\$59,116
See <u>Notes to Consolidated Financial Statements</u> .				

THE LACLEDE GROUP, INC.
CONSOLIDATED BALANCE SHEETS
(UNAUDITED)

(Thousands)	Mar. 31, 2013	Sept. 30, 2012	Mar. 31, 2012
ASSETS			
Utility Plant	\$1,538,890	\$1,497,419	\$1,425,922
Less: Accumulated depreciation and amortization	478,971	478,120	468,209
Net Utility Plant	1,059,919	1,019,299	957,713
Non-utility property	5,456	6,039	4,448
Other investments	52,910	50,775	54,688
Other Property and Investments	58,366	56,814	59,136
Current Assets:			
Cash and cash equivalents	146,880	27,457	9,302
Accounts receivable:			
Utility	148,624	64,027	100,015
Non-utility	55,925	51,042	34,915
Other	9,290	26,478	18,666
Allowance for doubtful accounts	(8,833)	(7,705)	(8,758)
Delayed customer billings	19,663	—	13,464
Inventories:			
Natural gas stored underground	32,776	92,729	57,456
Propane gas	8,963	10,200	8,964
Materials and supplies at average cost	4,385	3,543	4,102
Natural gas receivable	13,470	22,377	16,351
Derivative instrument assets	6,021	2,855	5,297
Unamortized purchased gas adjustments	11,039	40,674	11,241
Deferred income taxes	2,527	—	—
Prepayments and other	9,183	9,339	6,795
Total Current Assets	459,913	343,016	277,810
Deferred Charges:			
Regulatory assets	424,743	456,047	457,749
Other	6,157	5,086	5,723
Total Deferred Charges	430,900	461,133	463,472
Total Assets	\$2,009,098	\$1,880,262	\$1,758,131

THE LACLEDE GROUP, INC.
CONSOLIDATED BALANCE SHEETS (Continued)
(UNAUDITED)

(Thousands, except share amounts)	Mar. 31, 2013.	Sept. 30, 2012.	Mar. 31, 2012
CAPITALIZATION AND LIABILITIES			
Capitalization:			
Common stock (70,000,000 shares authorized, 22,643,693, 22,539,431, and 22,489,986 shares issued, respectively)	\$22,644	\$22,539	\$22,490
Paid-in capital	172,736	168,607	165,056
Retained earnings	451,114	414,581	425,500
Accumulated other comprehensive loss	(6,491)	(4,116)	2,158
Total Common Stock Equity	640,003	601,611	615,204
Long-term debt (less current portion)	464,434	339,416	339,386
Total Capitalization	1,104,437	941,027	954,590
Current Liabilities:			
Notes payable	—	40,100	—
Accounts payable	108,648	89,503	73,045
Advance customer billings	—	25,146	—
Current portion of long-term debt	—	25,000	25,000
Wages and compensation accrued	16,175	13,908	13,873
Dividends payable	10,059	9,831	9,697
Customer deposits	7,706	8,565	9,459
Interest accrued	6,191	8,590	8,789
Taxes accrued	44,550	11,304	25,062
Deferred income taxes	—	6,675	6,615
Other	14,015	13,502	16,220
Total Current Liabilities	207,344	252,124	187,760
Deferred Credits and Other Liabilities:			
Deferred income taxes	343,016	355,509	335,215
Unamortized investment tax credits	3,006	3,113	3,219
Pension and postretirement benefit costs	191,778	196,558	163,940
Asset retirement obligations	41,512	40,368	28,313
Regulatory liabilities	83,026	56,319	53,267
Other	34,979	35,244	31,827
Total Deferred Credits and Other Liabilities	697,317	687,111	615,781
Commitments and Contingencies (Note 11)			
Total Capitalization and Liabilities	\$2,009,098	\$1,880,262	\$1,758,131
See Notes to Consolidated Financial Statements .			

THE LACLEDE GROUP, INC.
 STATEMENTS OF CONSOLIDATED CASH FLOWS
 (UNAUDITED)

	Six Months Ended March 31,	
(Thousands)	2013	2012
Operating Activities:		
Net Income	\$55,810	\$54,858
Adjustments to reconcile net income to net cash provided by (used in) operating activities:		
Depreciation, amortization, and accretion	22,913	20,565
Deferred income taxes and investment tax credits	(11,132)	6,167
Other – net	450	(744)
Changes in assets and liabilities:		
Accounts receivable – net	(71,164)	(20,355)
Unamortized purchased gas adjustments	29,635	14,478
Deferred purchased gas costs	43,827	(30,160)
Accounts payable	23,797	(26,546)
Delayed customer billings - net	(44,809)	(28,694)
Taxes accrued	32,971	12,575
Natural gas stored underground	59,953	57,714
Other assets and liabilities	115	11,601
Net cash provided by operating activities	142,366	71,459
Investing Activities:		
Capital expenditures	(62,707)	(40,658)
Other investments	(2,126)	(1,440)
Net cash used in investing activities	(64,833)	(42,098)
Financing Activities:		
Issuance of long-term debt	125,000	—
Maturity of first mortgage bonds	(25,000)	—
Repayment of short-term debt – net	(40,100)	(46,000)
Changes in book overdrafts	(1,262)	357
Issuance of common stock	2,852	2,195
Non-employee directors' restricted stock awards	—	(565)
Dividends paid	(19,054)	(18,314)
Employees' taxes paid associated with restricted shares withheld upon vesting	(729)	(1,165)
Excess tax benefits from stock-based compensation	636	185
Other	(453)	(29)
Net cash provided by (used in) financing activities	41,890	(63,336)
Net Increase (Decrease) in Cash and Cash Equivalents	119,423	(33,975)
Cash and Cash Equivalents at Beginning of Period	27,457	43,277
Cash and Cash Equivalents at End of Period	\$146,880	\$9,302
Supplemental Disclosure of Cash Paid (Refunded) During the Period for:		
Interest	\$14,569	\$12,521
Income taxes	(3,165)	2,763

See Notes to Consolidated Financial Statements.

THE LACLEDE GROUP, INC.
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
(UNAUDITED)

1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

These notes are an integral part of the accompanying unaudited consolidated financial statements of The Laclede Group, Inc. (Laclede Group or the Company) and its subsidiaries. In the opinion of Laclede Group, this interim report includes all adjustments (consisting of only normal recurring accruals) necessary for the fair presentation of the results of operations for the periods presented. This Form 10-Q should be read in conjunction with the Notes to Consolidated Financial Statements contained in the Company's Fiscal Year 2012 Form 10-K.

The consolidated financial position, results of operations, and cash flows of Laclede Group are comprised primarily from the financial position, results of operations, and cash flows of Laclede Gas Company (Laclede Gas or the Utility). Laclede Gas is a regulated natural gas distribution utility having a material seasonal cycle. As a result, these interim statements of income for Laclede Group are not necessarily indicative of annual results or representative of succeeding quarters of the fiscal year. Due to the seasonal nature of the business of Laclede Gas, earnings are typically concentrated in the November through April period, which generally corresponds with the heating season. Laclede Energy Resources, Inc. (LER) includes its wholly owned subsidiary, LER Storage Services, Inc., which became operational on January 1, 2012.

REVENUE RECOGNITION - Laclede Gas reads meters and bills its customers on monthly cycles. The Utility records its gas utility revenues from gas sales and transportation services on an accrual basis that includes estimated amounts for gas delivered, but not yet billed. The accruals for unbilled revenues are reversed in the subsequent accounting period when meters are actually read and customers are billed. The amounts of accrued unbilled revenues at March 31, 2013 and 2012, for the Utility, were \$33.3 million and \$13.0 million, respectively. The amount of accrued unbilled revenue at September 30, 2012 was \$11.6 million.

GROSS RECEIPTS TAXES - Gross receipts taxes associated with Laclede Gas' natural gas utility service are imposed on the Utility and billed to its customers. These amounts are recorded gross in the Statements of Consolidated Income. Amounts recorded in Gas Utility Operating Revenues for the quarters ended March 31, 2013 and 2012 were \$17.2 million and \$15.5 million, respectively. Amounts recorded in Gas Utility Operating Revenues for the six months ended March 31, 2013 and 2012 were \$27.5 million and \$25.7 million, respectively. Gross receipts taxes are expensed by the Utility and included in the Taxes, other than income taxes line.

NEW ACCOUNTING STANDARDS - In June 2011, the Financial Accounting Standards Board (FASB) issued Accounting Standards Update (ASU) No. 2011-05, "Presentation of Comprehensive Income," to amend ASC Topic 220, "Comprehensive Income," by changing certain financial statement presentation requirements. Under the amended guidance, entities may either present a single continuous statement of comprehensive income or, consistent with the Company's current presentation, provide separate but consecutive statements (a statement of income and a statement of comprehensive income). ASU No. 2011-05 would have required that, regardless of the method chosen, reclassification adjustments from other comprehensive income to net income be presented on the face of the financial statements, displaying the effect on both net income and other comprehensive income. However, in December 2011, the FASB issued ASU No. 2011-12 to defer the effective date of this particular requirement while it reconsiders this provision of the guidance. The amendments in these ASUs do not change the items that are required to be reported in other comprehensive income and, accordingly, did not impact total net income, comprehensive income, or earnings per share upon adoption in the first quarter of fiscal year 2013.

In December 2011, the FASB issued ASU No. 2011-11, "Disclosures about Offsetting Assets and Liabilities," to amend ASC Topic 210, "Balance Sheet," to require additional disclosures about financial instruments and derivative instruments that have been presented on a net basis (offset) in the balance sheet. Additionally, information about financial instruments and derivative instruments that are subject to enforceable master netting arrangements or similar agreements, irrespective of whether they are presented net in the balance sheet, is required to be disclosed. The ASU impacts disclosures only and will not require any changes to financial statement presentation. The Company will present the new disclosures retrospectively beginning in the first quarter of fiscal year 2014.

In February 2013, the FASB issued ASU No. 2013-02, "Reporting of Amounts Reclassified Out of Accumulated Other Comprehensive Income." This ASU amends Accounting Standards Codification (ASC) Topic 220, "Comprehensive Income," by requiring entities to provide information about the amounts reclassified out of accumulated other comprehensive income by component. In addition, an entity is required to provide information on significant amounts reclassified out of accumulated other comprehensive income by the respective line items of net income, but only if the amount reclassified is required under U.S. GAAP to be reclassified to net income in its entirety in the same reporting period. The Company will present the new disclosures prospectively beginning in the first quarter of fiscal year 2014.

2. PENSION PLANS AND OTHER POSTRETIREMENT BENEFITS

Pension Plans

Laclede Gas has non-contributory, defined benefit, trustee forms of pension plans covering substantially all employees. Plan assets consist primarily of corporate and U.S. government obligations and a growth segment consisting of exposure to equity markets, commodities, real estate and inflation-indexed securities, achieved through derivative instruments.

Pension costs for quarters ended March 31, 2013 and 2012 were \$4.2 million and \$7.6 million, respectively, including amounts charged to construction. Pension costs for six months ended March 31, 2013 and 2012 were \$8.4 million and \$11.8 million, respectively, including amounts charged to construction.

The net periodic pension costs include the following components:

(Thousands)	Three Months Ended March 31,		Six Months Ended March 31,	
	2013	2012	2013	2012
Service cost – benefits earned during the period	\$2,311	\$2,301	\$4,622	\$4,613
Interest cost on projected benefit obligation	4,066	4,840	8,132	9,711
Expected return on plan assets	(4,741)	(4,899)	(9,482)	(9,798)
Amortization of prior service cost	136	148	272	296
Amortization of actuarial loss	2,839	2,259	5,678	4,536
Loss on lump-sum settlement	—	3,407	—	3,407
Sub-total	4,611	8,056	9,222	12,765
Regulatory adjustment	(433)	(484)	(867)	(967)
Net pension cost	\$4,178	\$7,572	\$8,355	\$11,798

Pursuant to the provisions of the Laclede Gas pension plans, pension obligations may be satisfied by lump-sum cash payments. Pursuant to a Missouri Public Service Commission (MoPSC or Commission) Order, lump-sum payments are recognized as settlements (which can result in gains or losses) only if the total of such payments exceeds 100% of the sum of service and interest costs. There were no lump-sum payments recognized as settlements during the six months ended March 31, 2013. Lump-sum payments recognized as settlements were \$6.4 million during the six months ended March 31, 2012.

Pursuant to a MoPSC Order, the return on plan assets is based on the market-related value of plan assets implemented prospectively over a four-year period. Gains or losses not yet includible in pension cost are amortized only to the extent that such gain or loss exceeds 10% of the greater of the projected benefit obligation or the market-related value of plan assets. Such excess is amortized over the average remaining service life of active participants. The recovery in rates for the Utility's qualified pension plans is based on an annual allowance of \$15.5 million effective January 1, 2011. The difference between these amounts and pension expense as calculated pursuant to the above and that otherwise would be included in the Statements of Consolidated Income and Statements of Consolidated Comprehensive Income is deferred as a regulatory asset or regulatory liability.

The funding policy of Laclede Gas is to contribute an amount not less than the minimum required by government funding standards, nor more than the maximum deductible amount for federal income tax purposes. Fiscal year 2013 contributions to the pension plans through March 31, 2013 were \$8.9 million to the qualified trusts and approximately \$0.3 million to the non-qualified plans. Contributions to the pension plans for the remaining six months of fiscal 2013 are anticipated to be at least \$14.5 million to the qualified trusts and \$0.8 million to the non-qualified plans.

Postretirement Benefits

Laclede Gas provides certain life insurance benefits at retirement. Medical insurance is available after early retirement until age 65. The transition obligation not yet includible in postretirement benefit cost is being amortized over 20

years. Postretirement benefit costs for both the quarters ended March 31, 2013 and 2012 were \$2.4 million, including amounts charged to construction. Postretirement benefit costs for both the six months ended March 31, 2013 and 2012 were \$4.8 million, including amounts charged to construction.

Net periodic postretirement benefit costs consisted of the following components:

(Thousands)	Three Months Ended March 31,		Six Months Ended March 31,	
	2013	2012	2013	2012
Service cost – benefits earned during the period	\$2,534	\$2,015	\$5,067	\$4,030
Interest cost on accumulated postretirement benefit obligation	1,279	1,380	2,558	2,760
Expected return on plan assets	(1,081)	(991)	(2,162)	(1,982)
Amortization of transition obligation	23	34	46	68
Amortization of prior service cost (credit)	1	(518)	2	(1,036)
Amortization of actuarial loss	1,325	1,065	2,650	2,130
Sub-total	4,081	2,985	8,161	5,970
Regulatory adjustment	(1,699)	(604)	(3,398)	(1,208)
Net postretirement benefit cost	\$2,382	\$2,381	\$4,763	\$4,762

Missouri state law provides for the recovery in rates of costs accrued pursuant to GAAP provided that such costs are funded through an independent, external funding mechanism. Laclede Gas established Voluntary Employees' Beneficiary Association (VEBA) and Rabbi trusts as its external funding mechanisms. VEBA and Rabbi trusts' assets consist primarily of money market securities and mutual funds invested in stocks and bonds.

Pursuant to a MoPSC Order, the return on plan assets is based on the market-related value of plan assets implemented prospectively over a four-year period. Gains and losses not yet includible in postretirement benefit cost are amortized only to the extent that such gain or loss exceeds 10% of the greater of the accumulated postretirement benefit obligation or the market-related value of plan assets. Such excess is amortized over the average remaining service life of active participants. The recovery in rates for the Utility's postretirement benefit plans is based on an annual allowance of \$9.5 million effective January 1, 2011. The difference between these amounts and postretirement benefit cost based on the above and that otherwise would be included in the Statements of Consolidated Income and Statements of Consolidated Comprehensive Income is deferred as a regulatory asset or regulatory liability.

Laclede Gas' funding policy is to contribute amounts to the trusts equal to the periodic benefit cost calculated pursuant to GAAP as recovered in rates. Fiscal year 2013 contributions to the postretirement plans through March 31, 2013 were \$4.1 million to the qualified trusts and approximately \$0.4 million paid directly to participants from Laclede Gas' funds. Contributions to the postretirement plans for the remaining six months of fiscal year 2013 are anticipated to be \$12.2 million to the qualified trusts and \$0.4 million paid directly to participants from Laclede Gas' funds.

3. STOCK-BASED COMPENSATION

Awards of stock-based compensation are made pursuant to The Laclede Group 2006 Equity Incentive Plan (2006 Plan). Refer to Note 3 of the Consolidated Financial Statements included in the Company's Form 10-K for the fiscal year ended September 30, 2012 for descriptions of the plan.

Restricted Stock Awards

During the six months ended March 31, 2013, the Company granted 108,419 performance-contingent restricted stock units to executive officers and key employees at a weighted average grant date fair value of \$34.48 per share. This number represents the maximum shares that can be earned pursuant to the terms of the awards. Most of these stock units have a performance period ending September 30, 2015. While the participants have no interim voting rights on these stock units, dividends accrue during the performance period and are paid to the participants upon vesting, but are subject to forfeiture if the underlying stock units do not vest. The number of stock units that will ultimately vest is dependent upon the attainment of certain levels of earnings and other strategic goals, as well as the Company's level of total shareholder return (TSR) during the performance period relative to a comparator group of companies. This TSR

provision is considered a market condition under GAAP.

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Activity of restricted stock and restricted stock units subject to performance and/or market conditions during the six months ended March 31, 2013 is presented below:

	Restricted Stock/ Stock Units	Weighted Average Grant Date Fair Value
Nonvested at September 30, 2012	232,403	\$30.89
Granted (maximum shares that can be earned)	108,419	\$34.48
Vested	(37,436)	) \$27.02
Forfeited	(48,782)	) \$25.71
Nonvested at March 31, 2013	254,604	\$33.98

During the six months ended March 31, 2013, the Company granted 58,774 shares of time-vested restricted stock and stock units to executive officers, key employees, and directors at a weighted average grant date fair value of \$39.96 per share. Most of these shares were awarded on December 3, 2012 and vest December 3, 2015. In the interim, participants receive full voting rights and dividends, which are not subject to forfeiture.

Time-vested restricted stock and stock unit activity for the six months ended March 31, 2013 is presented below:

	Restricted Stock/ Stock Units	Weighted Average Grant Date Fair Value
Nonvested at September 30, 2012	115,115	\$36.54
Granted	58,774	\$39.96
Vested	(20,200)	) \$30.46
Forfeited	(3,250)	) \$38.18
Nonvested at March 31, 2013	150,439	\$38.65

During the six months ended March 31, 2013, 57,636 shares of restricted stock and stock units (performance-contingent and time-vested), awarded on November 4, 2009, December 1, 2009, and January 4, 2010, vested. The Company withheld 18,744 of the vested shares at a weighted average price of \$38.90 per share pursuant to elections by employees to satisfy tax withholding obligations.

Stock Option Awards

Stock option activity for the six months ended March 31, 2013 is presented below:

	Stock Options	Weighted Average Exercise Price	Weighted Average Remaining Contractual Term (Years)	Aggregate Intrinsic Value (\$000)
Outstanding at September 30, 2012	214,000	\$31.02		
Granted	—	\$—		
Exercised	(49,500)	) \$29.54		
Forfeited	—	\$—		
Expired	—	\$—		

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Outstanding at March 31, 2013	164,500	\$31.47	2.1	\$1,848
Fully Vested and Expected to Vest at March 31, 2013	164,500	\$31.47	2.1	\$1,848
Exercisable at March 31, 2013	164,500	\$31.47	2.1	\$1,848

The closing price of the Company's common stock was \$42.70 at March 31, 2013.

Equity Compensation Costs

The amounts of compensation cost recognized for share-based compensation arrangements are presented below:

(Thousands)	Three Months Ended March 31,		Six Months Ended March 31,	
	2013	2012	2013	2012
Total equity compensation cost	\$1,137	\$684	\$1,759	\$1,351
Compensation cost capitalized	(356)	(221)	(539)	(359)
Compensation cost recognized in net income	781	463	1,220	992
Income tax benefit recognized in net income	(298)	(179)	(467)	(383)
Compensation cost recognized in net income, net of income tax	\$483	\$284	\$753	\$609

As of March 31, 2013, there was \$7.1 million of total unrecognized compensation cost related to nonvested share-based compensation arrangements. That cost is expected to be recognized over a weighted average period of 2.2 years.

4. EARNINGS PER COMMON SHARE

(Thousands, Except Per Share Amounts)	Three Months Ended March 31,		Six Months Ended March 31,	
	2013	2012	2013	2012
Basic EPS:				
Net Income	\$30,242	\$29,684	\$55,810	\$54,858
Less: Income allocated to participating securities	186	167	312	324
Net Income Available to Common Shareholders	\$30,056	\$29,517	\$55,498	\$54,534
Weighted Average Shares Outstanding	22,421	22,254	22,396	22,223
Earnings Per Share of Common Stock	\$1.34	\$1.33	\$2.48	\$2.45
Diluted EPS:				
Net Income	\$30,242	\$29,684	\$55,810	\$54,858
Less: Income allocated to participating securities	186	166	311	323
Net Income Available to Common Shareholders	\$30,056	\$29,518	\$55,499	\$54,535
Weighted Average Shares Outstanding	22,421	22,254	22,396	22,223
Dilutive Effect of Stock Options, Restricted Stock, and Restricted Stock Units	77	82	70	76
Weighted Average Diluted Shares	22,498	22,336	22,466	22,299
Earnings Per Share of Common Stock	\$1.34	\$1.32	\$2.47	\$2.45
Outstanding Shares Excluded from the Calculation of Diluted EPS Attributable to: Restricted stock and stock units subject to performance and/or market conditions	211	203	211	203

5. FAIR VALUE OF FINANCIAL INSTRUMENTS

The carrying amounts and estimated fair values of financial instruments not measured at fair value on a recurring basis are as follows:

(Thousands)	Carrying Amount	Fair Value	Classification of Estimated Fair Value		
			Quoted Prices in Active Markets (Level 1)	Significant Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)
As of March 31, 2013					
Cash and cash equivalents	\$ 146,880	\$ 146,880	\$ 136,826	\$ 10,054	\$ —
Short-term debt	—	—	—	—	—
Long-term debt, including current portion	464,434	539,260	—	539,260	—
As of September 30, 2012					
Cash and cash equivalents	\$ 27,457	\$ 27,457	\$ 17,380	\$ 10,077	\$ —
Short-term debt	40,100	40,100	—	40,100	—
Long-term debt, including current portion	364,416	452,768	—	452,768	—
As of March 31, 2012					
Cash and cash equivalents	\$ 9,302	\$ 9,302	\$ 4,261	\$ 5,041	\$ —
Short-term debt	—	—	—	—	—
Long-term debt, including current portion	364,386	432,098	—	432,098	—

The carrying amounts for cash and cash equivalents and short-term debt approximate fair value due to the short maturity of these instruments. The fair values of long-term debt are estimated based on market prices for similar issues. Refer to Note 6, Fair Value Measurements, for information on financial instruments measured at fair value on a recurring basis.

6. FAIR VALUE MEASUREMENTS

The following table categorizes the assets and liabilities in the Consolidated Balance Sheets that are accounted for at fair value on a recurring basis in periods subsequent to initial recognition.

(Thousands)	Quoted Prices in Active Markets (Level 1)	Significant Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)	Effects of Netting and Cash Margin Receivables /Payables	Total
As of March 31, 2013					
Assets					
U. S. Stock/Bond Mutual Funds	\$ 13,922	\$—	\$—	\$—	\$ 13,922
NYMEX/ICE natural gas contracts	11,010	379	—	(8,209	) 3,180
NYMEX gasoline and heating oil contracts	322	—	—	(192	) 130
Natural gas commodity contracts	—	2,888	117	(289	) 2,716
Total	\$ 25,254	\$ 3,267	\$ 117	\$ (8,690	) \$ 19,948
Liabilities					
NYMEX/ICE natural gas contracts	\$ 2,447	\$ 1,342	\$—	\$ (3,789	) \$—
Natural gas commodity contracts	—	990	24	(289	) 725
Interest rate swaps	\$—	\$ 4,549	\$—	\$—	\$ 4,549
Total	\$ 2,447	\$ 6,881	\$ 24	\$ (4,078	) \$ 5,274
As of September 30, 2012					
Assets					
U. S. Stock/Bond Mutual Funds	\$ 13,187	\$—	\$—	\$—	\$ 13,187
NYMEX/ICE natural gas contracts	7,411	994	—	(8,405	) —
NYMEX gasoline and heating oil contracts	344	—	—	(344	) —
Natural gas commodity contracts	—	3,060	113	(299	) 2,874
Total	\$ 20,942	\$ 4,054	\$ 113	\$ (9,048	) \$ 16,061
Liabilities					
NYMEX/ICE natural gas contracts	\$ 12,253	\$ 1,891	\$—	\$ (14,144	) \$—
Natural gas commodity contracts	—	428	4	(299	) 133
Total	\$ 12,253	\$ 2,319	\$ 4	\$ (14,443	) \$ 133
As of March 31, 2012					
Assets					
U. S. Stock/Bond Mutual Funds	\$ 17,907	\$—	\$—	\$—	\$ 17,907
NYMEX/ICE natural gas contracts	5,182	1,310	—	(4,881	) 1,611
NYMEX gasoline and heating oil contracts	81	—	—	(81	) —
Natural gas commodity contracts	—	4,362	79	(538	) 3,903
Total	\$ 23,170	\$ 5,672	\$ 79	\$ (5,500	) \$ 23,421
Liabilities					
NYMEX/ICE natural gas contracts	\$ 37,811	\$ 2,342	\$—	\$ (40,153	) \$—
Natural gas commodity contracts	—	1,190	21	(538	) 673
Total	\$ 37,811	\$ 3,532	\$ 21	\$ (40,691	) \$ 673

The mutual funds included in Level 1 are valued based on exchange-quoted market prices of identical securities. Derivative instruments included in Level 1 are valued using quoted market prices on the New York Mercantile Exchange (NYMEX). Derivative instruments classified in Level 2 include physical commodity derivatives that are valued using broker or dealer quotation services whose prices are derived principally from, or are corroborated by, observable market inputs. Also included in Level 2 are certain derivative instruments that have values that are similar to, and correlate with, quoted prices for exchange-traded instruments in active markets. Derivative instruments included in Level 3 are valued using generally unobservable inputs that are based upon the best information available and reflect management's assumptions about how market participants would price the asset or liability. The Company's policy is to recognize transfers between the levels of the fair value hierarchy, if any, as of the beginning of the interim reporting period in which circumstances change or events occur to cause the transfer. The following is a reconciliation of the Level 3 beginning and ending net derivative balances:

	Three Months Ended March 31,		Six Months Ended March 31,	
(Thousands)	2013	2012	2013	2012
Beginning of period	\$30	\$37	\$109	\$13
Settlements	37	(41)	(29)	(7)
Net losses related to derivatives not held at end of period	—	(1)	—	(4)
Net gains related to derivatives still held at end of period	26	63	13	56
End of period	\$93	\$58	\$93	\$58

The mutual funds are included in the Other investments line of the Consolidated Balance Sheets. Derivative assets and liabilities, including receivables and payables associated with cash margin requirements, are presented net in the Consolidated Balance Sheets when a legally enforceable netting agreement exists between the Company and the counterparty to a derivative contract. For additional information on derivative instruments, see Note 7, Derivative Instruments and Hedging Activities.

7. DERIVATIVE INSTRUMENTS AND HEDGING ACTIVITIES

Laclede Gas has a risk management policy that allows for the purchase of natural gas derivative instruments with the goal of managing price risk associated with purchasing natural gas on behalf of its customers. This policy prohibits speculation and permits the Utility to hedge up to 70% of its normal volumes purchased for up to a 36-month period. Costs and cost reductions, including carrying costs, associated with the Utility's use of natural gas derivative instruments are allowed to be passed on to the Utility's customers through the operation of its Purchased Gas Adjustment (PGA) Clause, through which the MoPSC allows the Utility to recover gas supply costs, subject to prudence review by the MoPSC. Accordingly, Laclede Gas does not expect any adverse earnings impact as a result of the use of these derivative instruments. The Utility does not designate these instruments as hedging instruments for financial reporting purposes because gains or losses associated with the use of these derivative instruments are deferred and recorded as regulatory assets or regulatory liabilities pursuant to ASC Topic 980, "Regulated Operations," and, as a result, have no direct impact on the Statements of Consolidated Income. The timing of the operation of the PGA Clause may cause interim variations in short-term cash flows, because the Utility is subject to cash margin requirements associated with changes in the values of these instruments. Nevertheless, carrying costs associated with such requirements are recovered through the PGA Clause.

From time to time, Laclede Gas purchases NYMEX futures and options contracts to help stabilize operating costs associated with forecasted purchases of gasoline and diesel fuels used to power vehicles and equipment used in the course of its business. At March 31, 2013, Laclede Gas held 0.5 million gallons of gasoline futures contracts at an average price of \$2.30 per gallon. Most of these contracts, the longest of which extends to April 2014, are designated as cash flow hedges of forecasted transactions pursuant to ASC Topic 815. The gains or losses on these derivative

instruments are not subject to the Utility's PGA Clause.

In the course of its business, Laclede Group's gas marketing subsidiary, LER, which includes its wholly owned subsidiary LER Storage Services, Inc., enters into commitments associated with the purchase or sale of natural gas. Certain of LER's derivative natural gas contracts are designated as normal purchases or normal sales and, as such, are excluded from the scope of ASC Topic 815 and are accounted for as executory contracts on an accrual basis. Any of LER's derivative natural gas contracts that are not designated as normal purchases or normal sales are accounted for at fair value. At March 31, 2013, the fair values of 69.6 million MMBtu of non-exchange traded natural gas commodity contracts were reflected in the Consolidated Balance Sheet. Of these contracts, 59.8 million MMBtu will settle during fiscal year 2013, while the remaining 9.8 million MMBtu will settle during fiscal year 2014. These contracts have not been designated as hedges; therefore, changes in the fair value of these contracts are reported in earnings each period. Furthermore, LER manages the price risk associated with its fixed-priced commitments by either closely matching the offsetting physical purchase or sale of natural gas at fixed prices or through the use of NYMEX or Ice Clear Europe (ICE) futures, swap, and option contracts to lock in margins. At March 31, 2013, LER's unmatched fixed-price positions were not material to Laclede Group's financial position or results of operations. LER's NYMEX and ICE natural gas futures, swap, and option contracts used to lock in margins may be designated as cash flow hedges of forecasted transactions for financial reporting purposes.

The Company's exchange-traded/cleared derivative instruments consist primarily of NYMEX and ICE positions. The NYMEX is the primary national commodities exchange on which natural gas derivatives are traded. Open NYMEX/ICE natural gas futures and swap positions at March 31, 2013 were as follows:

	Laclede Gas Company		Laclede Energy Resources, Inc.	
	MMBtu (millions)	Avg. Price Per MMBtu	MMBtu (millions)	Avg. Price Per MMBtu
Open short futures positions				
Fiscal 2013	—	\$—	4.36	\$3.61
Fiscal 2014	—	—	3.26	3.86
Open long futures positions				
Fiscal 2013	7.58	\$3.40	0.77	\$3.71
Fiscal 2014	4.87	3.97	0.65	3.01

At March 31, 2013, Laclede Gas and LER also had 14.2 million MMBtu and 1.5 million MMBtu, respectively, of other price mitigation in place through the use of NYMEX natural gas option-based strategies.

In February 2013, Laclede Group entered into certain interest rate swap agreements to effectively lock in interest rates on a portion of the long-term debt it anticipates issuing to finance its pending acquisition of Missouri Gas Energy (MGE). These derivative instruments have been designated as cash flow hedges of forecasted transactions. These forward starting swaps involve the payment of a fixed interest rate and the receipt of a floating interest rate (the London Interbank Offered Rate, also known as LIBOR) over the terms specified in the contracts. At March 31, 2013, the notional amount of interest rate swaps outstanding was \$355 million with stated maturities ranging from 2018 to 2043 and fixed interest rates ranging between 1.28% and 3.14%.

Derivative instruments designated as cash flow hedges of forecasted transactions are recognized on the Consolidated Balance Sheets at fair value and the change in the fair value of the effective portion of these hedge instruments is recorded, net of tax, in other comprehensive income (OCI). Accumulated other comprehensive income (AOCI) is a component of Total Common Stock Equity. Amounts are reclassified from AOCI into earnings when the hedged items affect net income, using the same revenue or expense category that the hedged item impacts. Based on market prices at March 31, 2013, it is expected that approximately \$3.1 million of pre-tax unrealized losses will be reclassified into the Statements of Consolidated Income during the next twelve months. Cash flows from hedging transactions are classified in the same category as the cash flows from the items that are being hedged in the Statements of Consolidated Cash Flows.

The Effect of Derivative Instruments on the Statements of Consolidated Income and Statements of Consolidated Comprehensive Income

	Location of Gain (Loss) Recorded in Income	Three Months Ended March 31,		Six Months Ended March 31,	
(Thousands)		2013	2012	2013	2012
Derivatives in Cash Flow Hedging Relationships					
Effective portion of gain (loss) recognized in OCI on derivatives:					
NYMEX/ICE natural gas contracts		\$(3,188)	\$5,023	\$(1,855)	\$8,020
NYMEX gasoline and heating oil contracts		147	83	203	133
Interest rate swaps		(4,549)	—	(4,549)	—
Total		\$(7,590)	\$5,106	\$(6,201)	\$8,153
Effective portion of gain (loss) reclassified from AOCI to income:					
NYMEX/ICE natural gas contracts	Gas Marketing Operating Revenues	\$302	\$4,048	\$(1,661)	\$10,788
	Gas Marketing Operating Expenses	(318)	(4,445)	(652)	(8,369)
Sub-total		(16)	(397)	(2,313)	2,419
NYMEX gasoline and heating oil contracts	Other Gas Utility Operating Expenses	38	(11)	85	3
Total		\$22	\$(408)	\$(2,228)	\$2,422
Ineffective portion of gain (loss) on derivatives recognized in income:					
NYMEX/ICE natural gas contracts	Gas Marketing Operating Revenues	\$(87)	\$50	\$(412)	\$69
	Gas Marketing Operating Expenses	(44)	(90)	(129)	(196)
Sub-total		(131)	(40)	(541)	(127)
NYMEX gasoline and heating oil contracts	Other Gas Utility Operating Expenses	(31)	28	(132)	34
Total		\$(162)	\$(12)	\$(673)	\$(93)
Derivatives Not Designated as Hedging Instruments *					
Gain (loss) recognized in income on derivatives:					
Natural gas commodity contracts	Gas Marketing Operating Revenues	\$1,745	\$1,557	\$775	\$790
	Gas Marketing Operating Expenses	—	—	—	687
NYMEX/ICE natural gas contracts	Gas Marketing Operating Revenues	(1,679)	1,478	(612)	1,548
	Gas Marketing Operating Expenses	—	30	—	30
NYMEX gasoline and heating oil contracts	Other Income and (Income Deductions) - Net	13	12	46	13
Total		\$79	\$3,077	\$209	\$3,068

Gains and losses on Laclede Gas' natural gas derivative instruments, which are not designated as hedging instruments for financial reporting purposes, are deferred pursuant to the Utility's PGA Clause and initially recorded as regulatory assets or regulatory liabilities. These gains and losses are excluded from the table above because they have no direct impact on the Statements of Consolidated Income. Such amounts are recognized in the Statements of Consolidated Income as a component of Gas Utility Natural and Propane Gas operating expenses when they are recovered through the PGA Clause and reflected in customer billings.

Fair Value of Derivative Instruments in the Consolidated Balance Sheet at March 31, 2013

Fair Value of Derivative Instruments in the Consolidated Balance Sheet at March 31, 2016						
(Thousands)	Asset Derivatives		*	Liability Derivatives		*
	Balance Sheet Location	Fair Value		Balance Sheet Location	Fair Value	
Derivatives designated as hedging instruments						
NYMEX/ICE natural gas contracts	Accounts Receivable - Other	\$520		Accounts Receivable - Other	\$2,993	
NYMEX/ICE natural gas contracts	Other Deferred Charges	5		Other Deferred Charges	—	
NYMEX gasoline and heating oil contracts	Derivative Instrument Assets	312		Derivative Instrument Assets	—	
Interest rate swaps	Other Current Liabilities	—		Other Current Liabilities	4,549	
Sub-total		837			7,542	
Derivatives not designated as hedging instruments						
NYMEX/ICE natural gas contracts	Derivative Instrument Assets	10,862		Derivative Instrument Assets	339	
	Accounts Receivable – Other	2		Accounts Receivable – Other	457	
Natural gas commodity contracts	Derivative Instrument Assets	2,943		Derivative Instrument Assets	227	
	Other Current Liabilities	62		Other Current Liabilities	787	
NYMEX gasoline and heating oil contracts	Derivative Instrument Assets	10		Derivative Instrument Assets	—	
Sub-total		13,879			1,810	
Total derivatives		\$14,716			\$9,352	

Fair Value of Derivative Instruments in the Consolidated Balance Sheet at September 30, 2012

Fair Value of Derivative Instruments in the Consolidated Balance Sheet at September 30, 2012						
	Asset Derivatives			Liability Derivatives		
(Thousands)	Balance Sheet Location	Fair Value	*	Balance Sheet Location	Fair Value	*
Derivatives designated as hedging instruments						
NYMEX/ICE natural gas contracts	Accounts Receivable - Other	\$405		Accounts Receivable - Other	\$3,413	
NYMEX gasoline and heating oil contracts	Accounts Receivable - Other	334		Accounts Receivable - Other	—	
Sub-total		739			3,413	
Derivatives not designated as hedging instruments						
NYMEX/ICE natural gas contracts	Accounts Receivable - Other	8,000		Accounts Receivable - Other	10,731	
Natural gas commodity contracts	Derivative Instrument Assets	3,150		Derivative Instrument Assets	295	
	Other Current Liabilities	4		Other Current Liabilities	137	
	Other Deferred Charges	19		Other Deferred Charges	—	
NYMEX gasoline and heating oil contracts	Accounts Receivable - Other	10		Accounts Receivable - Other	—	
Sub-total		11,183			11,163	
Total derivatives		\$11,922			\$14,576	

Fair Value of Derivative Instruments in the Consolidated Balance Sheet at March 31, 2012

Fair Value of Derivative Instruments in the Consolidated Balance Sheet at March 31, 2012						
	Asset Derivatives			Liability Derivatives		
(Thousands)	Balance Sheet Location	Fair Value	*	Balance Sheet Location	Fair Value	*
Derivatives designated as hedging instruments						
NYMEX/ICE natural gas contracts	Derivative Instrument Assets	\$3,545		Derivative Instrument Assets	\$3,242	
NYMEX gasoline and heating oil contracts	Accounts Receivable - Other	72		Accounts Receivable - Other	—	
Sub-total		3,617			3,242	
Derivatives not designated as hedging instruments						
NYMEX/ICE natural gas contracts	Accounts Receivable - Other	709		Accounts Receivable - Other	36,437	
	Derivative Instrument Assets	2,238		Derivative Instrument Assets	474	
Natural gas commodity contracts	Derivative Instrument Assets	4,176		Derivative Instrument Assets	490	
	Other Deferred Charges	217		Other Deferred Charges	—	
	Other Current Liabilities	48		Other Current Liabilities	721	
NYMEX gasoline and heating oil contracts	Accounts Receivable - Other	9		Accounts Receivable - Other	—	
Sub-total		7,397			38,122	
Total derivatives		\$11,014			\$41,364	

The fair values of Asset Derivatives and Liability Derivatives exclude the fair value of cash margin receivables or payables with counterparties subject to netting arrangements. Fair value amounts of derivative contracts (including the fair value amounts of cash margin receivables and payables) for which there is a legal right to set off are presented net on the Consolidated Balance Sheets. As such, the gross balances presented in the table above are not indicative of the Company's net economic exposure. Refer to Note 6, Fair Value Measurements, for information on the valuation of derivative instruments.

Following is a reconciliation of the amounts in the tables above to the amounts presented in the Consolidated Balance Sheets:

(Thousands)	Mar. 31, 2013	Sept. 30, 2012	Mar. 31, 2012
Fair value of asset derivatives presented above	\$14,716	\$11,922	\$11,014
Fair value of cash margin receivables offset with derivatives	2,928	5,478	35,648
Netting of assets and liabilities with the same counterparty	(11,618)	) (14,526	) (41,148
Total	\$6,026	\$2,874	\$5,514
Derivative Instrument Assets, per Consolidated Balance Sheets:			
Derivative instrument assets	\$6,021	\$2,855	\$5,297
Other deferred charges	5	19	217
Total	\$6,026	\$2,874	\$5,514
Fair value of liability derivatives presented above	\$9,352	\$14,576	\$41,364

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Fair value of cash margin payables offset with derivatives	7,540	83	457
Netting of assets and liabilities with the same counterparty	(11,618	) (14,526	) (41,148
Derivative instrument liabilities, per Consolidated Balance Sheets*	\$5,274	\$133	\$673

* Included in the Other line of the Current Liabilities section

Additionally, at March 31, 2013, September 30, 2012, and March 31, 2012, the Company had \$1.3 million, \$10.0 million, and \$8.2 million, respectively, in cash margin receivables not offset with derivatives, that are presented in Accounts Receivable - Other.

8. CONCENTRATIONS OF CREDIT RISK

A significant portion of LER's transactions are with (or are associated with) energy producers, utility companies, and pipelines. These concentrations of transactions with these counterparties have the potential to affect the Company's overall exposure to credit risk, either positively or negatively, in that each of these three groups may be affected similarly by changes in economic, industry, or other conditions. To manage this risk, as well as credit risk from significant counterparties in these and other industries, LER has established procedures to determine the creditworthiness of its counterparties. These procedures include obtaining credit ratings and credit reports, analyzing counterparty financial statements to assess financial condition, and considering the industry environment in which the counterparty operates. This information is monitored on an ongoing basis. In some instances, LER may require credit assurances such as prepayments, letters of credit, or parental guarantees. In addition, LER may enter into netting arrangements to mitigate credit risk with counterparties in the energy industry from which LER both sells and purchases natural gas. Sales are typically made on an unsecured credit basis with payment due the month following delivery. Accounts receivable amounts are closely monitored and provisions for uncollectible amounts are accrued when losses are probable. To date, losses have not been significant. LER records accounts receivable, accounts payable, and prepayments for physical sales and purchases of natural gas on a gross basis. The amount included in accounts receivable attributable to energy producers and their marketing affiliates amounted to \$21.9 million at March 31, 2013. Net receivable amounts from these customers on the same date, reflecting netting arrangements, were \$19.5 million. Accounts receivable attributable to utility companies and their marketing affiliates comprised \$13.7 million of total accounts receivable at March 31, 2013, while net receivable amounts from these customers, reflecting netting arrangements, were \$11.6 million. LER also has concentrations of credit risk with certain individually significant counterparties. At March 31, 2013, the amounts included in accounts receivable from LER's five largest counterparties (in terms of net accounts receivable exposure), were \$23.9 million. These five counterparties are either investment-grade rated or owned by investment-grade rated companies. Net receivable amounts from these customers on the same date, reflecting netting arrangements, were \$22.4 million. Additionally, LER has concentrations of credit risk with pipeline companies associated with its natural gas receivable amounts.

9. OTHER INCOME AND (INCOME DEDUCTIONS) - NET

(Thousands)	Three Months Ended March 31,		Six Months Ended March 31,	
	2013	2012	2013	2012
Interest income	\$257	\$316	\$663	\$664
Net investment (loss) gain	1,174	1,164	1,104	2,194
Other income	9	11	77	11
Other income deductions	(100	) (110	) 580	451
Other Income and (Income Deductions) – Net	\$1,340	\$1,381	\$2,424	\$3,320

10. INFORMATION BY OPERATING SEGMENT

All of Laclede Group's subsidiaries are wholly owned. In the first quarter of fiscal year 2013, the Company retitled its segment names. The Gas Utility segment, previously titled Regulated Gas Distribution, consists of the regulated operations of Laclede Gas and is the core business segment of Laclede Group. Laclede Gas is a public utility engaged in the retail distribution and sale of natural gas serving an area in eastern Missouri, with a population of approximately 2.2 million, including the City of St. Louis and parts of ten counties in eastern Missouri. The Gas Marketing segment, previously titled Non-Regulated Gas Marketing, includes the results of LER, a subsidiary engaged in the non-regulated marketing of natural gas and related activities, and LER Storage Services, Inc., which became operational in January 2012 and utilizes natural gas storage contracts for providing natural gas sales. Other includes Laclede Pipeline Company's transportation of liquid propane regulated by the Federal Energy Regulatory Commission (FERC) as well as non-regulated activities, including, among other activities, real estate development, the compression of natural gas, and financial investments in other enterprises. These operations are conducted through seven subsidiaries. Other also includes Laclede Gas' non-regulated business activities, which are comprised of its propane storage and related services. Accounting policies are described in Note 1. Intersegment transactions include sales of natural gas from Laclede Gas to LER, propane storage services provided by Laclede Gas to Laclede Pipeline Company, sales of natural gas from LER to Laclede Gas, and propane transportation services provided by Laclede Pipeline Company to Laclede Gas.

Management evaluates the performance of the operating segments based on the computation of net economic earnings. Net economic earnings exclude from reported net income the after-tax impacts of net unrealized gains and losses and other timing differences associated with energy-related transactions. Net economic earnings also excludes the after-tax impact of costs related to unique acquisition, divestiture, and restructuring activities.

(Thousands)	Gas Utility	Gas Marketing	Other	Unallocated and Eliminations	Consolidated
Three Months Ended March 31, 2013					
Revenues from external customers	\$354,097	\$41,255	\$2,261	\$—	\$397,613
Intersegment revenues	9,814	(2,332)	) 319	(7,801)	) —
Total Operating Revenues	363,911	38,923	2,580	(7,801)	) 397,613
Net Economic Earnings (Losses)	30,197	2,368	(51)	) —	32,514
Total assets	1,821,372	202,012	126,668	(140,954)	) 2,009,098
Six Months Ended March 31, 2013					
Revenues from external customers	\$604,208	\$96,504	\$3,904	\$—	\$704,616
Intersegment revenues	10,494	4,574	578	(15,646)	) —
Total Operating Revenues	614,702	101,078	4,482	(15,646)	) 704,616
Net Economic Earnings (Losses)	55,538	5,649	(440)	) —	60,747
Total assets	1,821,372	202,012	126,668	(140,954)	) 2,009,098
Three Months Ended March 31, 2012					
Revenues from external customers	\$298,623	\$66,045	\$381	\$—	\$365,049
Intersegment revenues	—	1,927	259	(9,060)	) (6,874)
Total Operating Revenues	298,623	67,972	640	(9,060)	) 358,175
Net Economic Earnings	25,772	2,545	110	—	28,427
Total assets	1,680,948	177,129	151,646	(251,592)	) 1,758,131
Six Months Ended March 31, 2012					
Revenues from external customers	\$549,522	\$218,022	\$1,544	\$—	\$769,088
Intersegment revenues	3	8,538	519	(9,060)	) —

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Total Operating Revenues	549,525	226,560	2,063	(9,060	) 769,088
Net Economic Earnings	46,851	5,984	485	—	53,320
Total assets	1,680,948	177,129	151,646	(251,592	) 1,758,131

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Reconciliation of Consolidated Net Economic Earnings to Consolidated Net Income

	Three Months Ended		Six Months Ended		
	March 31,		March 31,		
(Thousands)	2013	2012	2013	2012	
Total Net Economic Earnings above	\$32,514	\$28,427	\$60,747	\$53,320	
Add: Unrealized (loss) gain on energy-related derivative contracts, net of tax	(587	) 1,963	(1,026	) 2,244	
Add: Lower of cost or market inventory adjustments, net of tax	—	(562	) —	(562	)
Add: Realized (loss) gain on economic hedges prior to sale of the physical commodity, net of tax	(9	) (144	) 22	(144	)
Add: Acquisition, divestiture, and restructuring activities, net of tax	(1,676	) —	(3,933	) —	
Net Income	\$30,242	\$29,684	\$55,810	\$54,858	

11. COMMITMENTS AND CONTINGENCIES

Commitments

Laclede Gas and LER have entered into various contracts, expiring on dates through fiscal year 2018, for the storage, transportation, and supply of natural gas. Minimum payments required under the contracts in place at March 31, 2013 are estimated at approximately \$410 million. Additional contracts are generally entered into prior to or during the heating season. Laclede Gas recovers its costs from customers in accordance with the PGA Clause.

During fiscal 2011, the Utility initiated a multi-year project to replace its existing customer relationship and work management, financial, and supply chain software applications to enhance its technology, customer service, and business processes. At March 31, 2013, the Company was contractually committed to costs of approximately \$1.5 million related to this project, with additional expenditures to be incurred throughout the project's life.

Refer to Note 12, Acquisition Agreements, for information about Laclede Group's commitments associated with the pending acquisitions of substantially all of the assets and liabilities of Missouri Gas Energy (MGE) and New England Gas Company (NEG) and the subsequent agreement with Algonquin Power & Utilities Corp. (APUC) that will allow an APUC subsidiary to acquire the Company's rights to purchase the assets of NEG.

Contingencies

Laclede Gas owns and operates natural gas distribution, transmission, and storage facilities, the operations of which are subject to various environmental laws, regulations, and interpretations. While environmental issues resulting from such operations arise in the ordinary course of business, such issues have not materially affected the Company's or Laclede Gas' financial position and results of operations. As environmental laws, regulations, and their interpretations change, however, Laclede Gas may be required to incur additional costs.

Similar to other natural gas utility companies, Laclede Gas faces the risk of incurring environmental liabilities. In the natural gas industry, these are typically associated with sites formerly owned or operated by gas distribution companies like Laclede Gas and/or its predecessor companies at which manufactured gas operations took place. At this time, Laclede Gas has identified three former manufactured gas plant (MGP) sites where costs have been incurred and claims have been asserted: one in Shrewsbury, Missouri and two in the City of St. Louis, Missouri.

With regard to the former MGP site located in Shrewsbury, Missouri, Laclede Gas and state and federal environmental regulators agreed upon certain remedial actions to a portion of the site in a 1999 Administrative Order on Consent (AOC), which actions have been completed. On September 22, 2008, EPA Region VII issued a letter of

Termination and Satisfaction terminating the AOC. However, if after this termination of the AOC, regulators require additional remedial actions, or additional claims are asserted, Laclede Gas may incur additional costs.

One of the sites located in the City of St. Louis is currently owned by a development agency of the City, which, together with other City development agencies, has selected a developer to redevelop the site. In conjunction with this redevelopment effort, Laclede Gas and another former owner of the site entered into an agreement (Remediation Agreement) with the City development agencies, the developer, and an environmental consultant that obligates one of the City agencies and the environmental consultant to remediate the site and obtain a No Further Action letter from the Missouri Department of Natural Resources. The Remediation Agreement also provides for a release of Laclede Gas and the other former site owner from certain liabilities related to the past and current environmental condition of the site and requires the developer and the environmental consultant to maintain certain insurance coverages, including remediation cost containment, premises pollution liability, and professional liability. The operative provisions of the Remediation Agreement were triggered on December 20, 2010, on which date Laclede Gas and the other former site owner, as full consideration under the Remediation Agreement, paid a small percentage of the cost of remediation of the site. The amount paid by Laclede Gas did not materially impact the financial condition, results of operations, or cash flows of the Company.

Laclede Gas has not owned the other site located in the City of St. Louis for many years. In a letter dated June 29, 2011, the Attorney General for the State of Missouri informed Laclede Gas that the Missouri Department of Natural Resources had completed an investigation of the site. The Attorney General requested that Laclede Gas participate in the follow up investigations of the site. In a letter dated January 10, 2012, the Company stated that it would participate in future environmental response activities at the site in conjunction with other potentially responsible parties that are willing to contribute to such efforts in a meaningful and equitable fashion. Further correspondence from the Missouri Attorney General dated April 12, 2012, and November 28, 2012, encouraged Laclede Gas and other present and former owners of the site to move forward with further site investigation for possible remediation via enrollment in the Missouri Department of Natural Resources Brownfields/Voluntary Cleanup Program (BVCP) in lieu of being subjected to enforcement action by the United States Environmental Protection Agency, Region VII. Accordingly, Laclede Gas and the other former and current owners of the site each have entered into, or are in the process of entering into, Provisional Cost Sharing and Environmental Response Agreements enabling Laclede Gas to enroll the property in the BVCP and to fund and conduct additional investigation of the property. Laclede Gas enrolled the site in the BVCP as of April 1, 2013.

To date, amounts required for remediation at these sites have not been material. However, the amount of costs relative to future remedial actions at these and other sites is unknown and may be material. Laclede Gas has notified its insurers that it seeks reimbursement for costs incurred in the past and future potential liabilities associated with the MGP sites. While some of the insurers have denied coverage and reserved their rights, Laclede Gas continues to discuss potential reimbursements with them. In 2005, the Utility's outside consultant completed an analysis of the MGP sites to determine cost estimates for a one-time contractual transfer of risk from each of the Utility's insurers of environmental coverage for the MGP sites. That analysis demonstrated a range of possible future expenditures to investigate, monitor, and remediate these MGP sites from \$5.8 million to \$36.3 million based upon then currently available facts, technology, and laws and regulations. The actual costs that Laclede Gas may incur could be materially higher or lower depending upon several factors, including whether remedial actions will be required, final selection and regulatory approval of any remedial actions, changing technologies and governmental regulations, the ultimate ability of other potentially responsible parties to pay, the successful completion of remediation efforts required by the Remediation Agreement described above, and any insurance recoveries. Costs associated with environmental remediation activities are accrued when such costs are probable and reasonably estimable.

Laclede Gas anticipates that any costs it may incur in the future to remediate these sites, less any amounts received as insurance proceeds or as contributions from other potentially responsible parties, would be deferred and recovered in rates through periodic adjustments approved by the MoPSC. Accordingly, any potential liabilities that may arise associated with remediating these sites are not expected to have a material impact on the future financial position and results of operations of Laclede Gas or the Company.

The MoPSC Staff previously proposed disallowances related to Laclede Gas' recovery of its purchased gas costs totaling \$6.0 million pertaining to Laclede Gas' purchase of gas from a marketing affiliate, LER, applicable to fiscal years 2005 through 2007. The MoPSC Staff also proposed a number of non-monetary recommendations, based on its review of gas costs for fiscal years 2008 through 2011. Laclede Gas believes that the proposed disallowances lack merit and is vigorously opposing these adjustments. Management, after discussion with counsel, continues to believe the final outcome of these matters will not have a material effect on the Company's financial position, results of operations, or cash flows. Laclede Gas is currently in discussions with the MoPSC Staff and other parties to resolve these matters.

In connection with its review of these affiliate transactions, Laclede Gas objected, on the grounds of relevance, to MoPSC data requests seeking to obtain from LER certain of LER's proprietary documents unrelated to Laclede Gas' purchases from LER. On July 7, 2010, the MoPSC Staff filed a complaint against Laclede Gas alleging that, by stating that it was not in possession of proprietary LER documents, Laclede Gas violated the MoPSC Order authorizing the holding company structure (2001 Order). Laclede Gas counterclaimed stating the Staff failed to adhere to pricing provisions of the MoPSC's affiliate transaction rules and Laclede Gas' Cost Allocation Manual. By orders dated November 3, 2010 and February 4, 2011, respectively, the MoPSC dismissed Laclede's counterclaim and granted summary judgment to Staff, finding that Laclede Gas violated the terms of the 2001 Order and authorizing its General Counsel to seek penalties in court against Laclede Gas. These Orders were later reversed by the Cole County Circuit Court, but ultimately upheld by the Western District Court of Appeals. On March 19, 2013, the Missouri Supreme Court declined Laclede Gas' request to review the opinion of the Western District Court of Appeals relating to the information-related requirements of the 2001 Order. As a result, additional LER documentation may need to be shared with the MoPSC staff. In addition, certain related complaints filed by the MoPSC Staff on October 6, 2010 and a counterclaim by Laclede Gas against Staff are still pending before the Commission. Management, after discussion with counsel, continues to believe the final outcome of these matters will not have a material effect on the Company's financial position, results of operations, or cash flows. Laclede Gas is currently in discussions with the MoPSC Staff and other parties to resolve these matters.

On June 29, 2010, the Office of Federal Contract Compliance Programs issued a Notice of Violations to Laclede Gas alleging lapses in certain employment selection procedures during a two-year period ending in February 2006. The Company believes that the allegations lack merit and is vigorously defending its position. Management, after discussion with counsel, believes that the final outcome of these matters will not have a material effect on the consolidated financial position and results of operations, or cash flows of the Company.

As discussed in Note 7, Derivative Instruments and Hedging Activities, Laclede Gas and LER enter into NYMEX and ICE exchange-traded/cleared derivative instruments. Previously, these instruments were held in accounts at MF Global, Inc. On October 31, 2011, affiliated entities of MF Global filed a Chapter 11 petition at the U.S. Bankruptcy Court in the Southern District of New York. Subsequently, the court-appointed bankruptcy trustee transferred all of the open positions and a significant portion of the margin deposits of Laclede Gas and LER to a new brokerage firm. On January 31, 2013, the bankruptcy trustee received approval from the court to make certain additional distributions to customers. As a result of this action, Laclede Gas and LER received partial cash distributions totaling \$0.7 million and \$0.1 million, respectively, in April 2013. As of April 29, 2013, Laclede Gas and LER had \$0.9 million and \$0.2 million, respectively, on deposit with MF Global that remain unavailable pending final resolution by the bankruptcy trustee. Regarding the funds that remain outstanding after this partial distribution, management is currently unable to predict when, or to what extent, these funds will be returned. Management does not believe that the Company's exposure is material.

Laclede Group is involved in other litigation, claims, and investigations arising in the normal course of business. Management, after discussion with counsel, believes that the final outcome will not have a material effect on the consolidated financial position, results of operations, or cash flows of the Company.

12. ACQUISITION AGREEMENTS

On December 14, 2012, Laclede Group entered into purchase and sale agreements, subject to customary closing adjustments, to acquire for \$1.035 billion (collectively, the Transaction) from Southern Union Company (SUG), an

affiliate of Energy Transfer Equity, L.P. and Energy Transfer Partners, L.P., substantially all of the assets and liabilities of SUG's MGE and NEG divisions (collectively, the Utilities). The Utilities are engaged in the distribution of natural gas on a regulated basis in western Missouri and in southeastern Massachusetts.

The Transaction is targeted to close before the end of fiscal year 2013, subject to customary closing conditions, including regulatory approvals from the MoPSC and the Massachusetts Department of Public Utilities. On January 22, 2013, the Federal Trade Commission notified the Company of the early termination of the waiting period under the Hart-Scott-Rodino Antitrust Improvements Act of 1976, as amended. No shareholder approval is required to complete the Transaction, and each of the entities has received all necessary approvals from their boards of directors.

The purchase and sale agreements contain certain termination rights for both the Company and SUG, including, among others, the right to terminate if the Transaction is not completed by October 14, 2013 (subject to up to four 30-day extensions under certain circumstances related to obtaining required regulatory approvals). In the event that SUG terminates the MGE acquisition agreement as a result of the failure of Laclede Group to obtain financing, the Company may be required to pay SUG a "reverse break up" fee of \$73.1 million, which amount will operate as liquidated damages and a cap on such liability for such breach.

Laclede Group's agreement to acquire MGE for \$975 million, via the newly formed wholly owned subsidiary Plaza Missouri Acquisition, Inc., was assigned by Laclede Group to Laclede Gas on January 11, 2013. Subsequently, on January 14, 2013, the Company filed an application with the MoPSC for approval to acquire the assets of MGE from SUG, and the Company continues to work with the MoPSC staff to respond to their requests for additional information supporting the Company's pending application.

Similarly, the agreement to acquire NEG for \$60 million, including approximately \$19.5 million of assumed NEG debt, is contracted through a second newly formed wholly owned subsidiary of Laclede Group, Plaza Massachusetts Acquisition, Inc. (Plaza Massachusetts). On February 11, 2013, the Company announced that it entered into an agreement with Algonquin Power & Utilities Corp. (APUC) that will allow an APUC subsidiary, through its acquisition of the stock of Plaza Massachusetts, to acquire the rights to purchase the assets of NEG, subject to certain approvals and conditions. Under the terms of this agreement, the Company will receive \$11 million from APUC at closing. Further, APUC has deposited \$3.0 million in an escrow account that will be paid to SUG at closing. The sale of NEG to APUC is subject to approval from the Massachusetts Department of Public Utilities (MDPU), and a filing that was made by the Company and SUG with the MDPU on January 24, 2013, for approval of the acquisition of NEG, was amended on February 19, 2013 to include APUC. On March 15, 2013, the MDPU issued a procedural schedule setting the case for hearing during the last week in June 2013. Laclede Group remains obligated to acquire NEG in the event that APUC is not able to satisfy all conditions for closing on or before October 14, 2013, although the Company believes this scenario would be unlikely. The Company's agreement with APUC is not anticipated to impact the MGE transaction.

The Transaction is supported by existing company cash and Laclede Group's fully committed \$1.020 billion bridge facility with Wells Fargo Bank, National Association. That bridge facility was syndicated to a group of nine financial institutions in January 2013. The Company anticipates permanent financing to be a combination of long-term debt and equity.

The Company continues to incur costs associated with the evaluation, approval and financing of the Transaction. During the three and six months ended March 31, 2013, Laclede Group recorded \$1.7 million and \$3.9 million, respectively, net of tax, of third-party expenses associated with the Transaction.

ITEM 2. MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

This management's discussion analyzes the financial condition and results of operations of The Laclede Group, Inc. (Laclede Group or the Company) and its subsidiaries. It includes management's view of factors that affect its business, explanations of past financial results including changes in earnings and costs from the prior year periods, and their effects on overall financial condition and liquidity.

Certain matters discussed in this report, excluding historical information, include forward-looking statements. Certain words, such as "may," "anticipate," "believe," "estimate," "expect," "intend," "plan," "seek," and similar words and expressions identify forward-looking statements that involve uncertainties and risks. Future developments may not be in accordance with our current expectations or beliefs and the effect of future developments may not be those anticipated. Among the factors that may cause results to differ materially from those contemplated in any forward-looking statement are:

- weather conditions and catastrophic events, particularly severe weather in the natural gas producing areas of the country;
- volatility in gas prices, particularly sudden and sustained changes in natural gas prices, including the related impact on margin deposits associated with the use of natural gas derivative instruments;
- the impact of changes and volatility in natural gas prices on our competitive position in relation to suppliers of alternative heating sources, such as electricity;
- changes in gas supply and pipeline availability, including decisions by natural gas producers to reduce production or shut in producing natural gas wells, expiration of existing supply and transportation arrangements that are not replaced with contracts with similar terms and pricing, as well as other changes that impact supply for and access to the markets in which our subsidiaries transact business;
- legislative, regulatory and judicial mandates and decisions, some of which may be retroactive, including those affecting
 - allowed rates of return
- incentive regulation
- industry structure
- purchased gas adjustment provisions
- rate design structure and implementation
- regulatory assets
- non-regulated and affiliate transactions
- franchise renewals
- environmental or safety matters, including the potential impact of legislative and regulatory actions related to climate change and pipeline safety
- taxes
- pension and other postretirement benefit liabilities and funding obligations
- accounting standards, including the effect of potential changes relative to adoption of or convergence with international accounting standards;
- the results of litigation;
- retention of, ability to attract, ability to collect from, and conservation efforts of, customers;
- capital and energy commodity market conditions, including the ability to obtain funds with reasonable terms for necessary capital expenditures and general operations and the terms and conditions imposed for obtaining sufficient gas supply;
- discovery of material weakness in internal controls; and
- employee workforce issues.

In addition, actual results may differ materially from those contemplated in any forward-looking statement due to the timing and likelihood of the closing of i) the purchase of substantially all of the assets and liabilities of Missouri Gas Energy (MGE) from Southern Union Company (SUG), ii) the Company's agreement with Algonquin Power & Utilities Corp. (APUC) to allow an APUC subsidiary to acquire the Company's rights to purchase the assets of New England Gas Company (NEG), and iii) the other factors discussed in "Risks Related To The Company's Acquisition Agreements With Southern Union Company And Algonquin Power & Utilities Corp." under Part II. Item 1A on page 45 of this Report. Refer to Acquisition Agreements on page 28 for additional information.

Readers are urged to consider the risks, uncertainties, and other factors that could affect our business as described in this report. All forward-looking statements made in this report rely upon the safe harbor protections provided under the Private Securities Litigation Reform Act of 1995. We do not, by including this statement, assume any obligation to review or revise any particular forward-looking statement in light of future events.

The Management's Discussion and Analysis of Financial Condition and Results of Operations should be read in conjunction with the Company's Consolidated Financial Statements and the Notes thereto.

ACQUISITION AGREEMENTS

In December 2012, Laclede Group, through two newly formed wholly owned subsidiaries, Plaza Missouri Acquisition, Inc. and Plaza Massachusetts Acquisition, Inc., entered into definitive purchase and sale agreements with SUG to acquire substantially all of the assets of MGE and NEG. On February 11, 2013, the Company announced that it entered into an agreement with APUC that will allow an APUC subsidiary to acquire the Company's rights to purchase the assets of NEG, subject to certain approvals and conditions. The Company's agreement with APUC is not expected to impact the MGE transaction. These transactions are targeted to be completed before the end of fiscal year 2013. The strategic rationale for Laclede Group is described below:

With a larger market capitalization and enterprise value, the Company expects to have improved trading liquidity and better access to the capital markets. It plans to be able to support growth initiatives in new markets with new customers.

Laclede Group will serve Missouri's two largest metropolitan areas in a state where it already has a working relationship with regulators.

The acquisition of MGE is expected to be neutral to Laclede Group's earnings per share in the first full year following closing and accretive thereafter. The acquisition of MGE is expected to be immediately accretive to cash flow.

Completion of the pending transactions, including the agreement with APUC relative to NEG, is subject to customary closing conditions, including regulatory approvals from the Missouri Public Service Commission (MoPSC or Commission) and the Massachusetts Department of Public Utilities. No shareholder approval is required to complete the transaction, and each of the entities has received all necessary approvals from their boards of directors. On January 22, 2013, the Federal Trade Commission notified the Company of the early termination of the waiting period under the Hart-Scott-Rodino Antitrust Improvements Act of 1976, as amended.

The purchase and sale agreements contain certain termination rights for both Laclede Group and SUG, and further provide for the payment of fees and expenses upon termination under specified circumstances. For additional information relating to the pending acquisitions, see Note 12, Acquisition Agreements, of the Notes of the Consolidated Financial Statements. Also refer to the Company's form 8-K filed on December 17, 2012. Subsequently, on January 11, 2013, the Company entered into an agreement to assign the MGE agreement to Laclede Group's Utility subsidiary, Laclede Gas, as described more fully in the Company's Form 8-K filed on January 14, 2013.

RESULTS OF OPERATIONS

Overview

Laclede Group's earnings are primarily derived from its Gas Utility segment, which reflects the regulated activities of its largest subsidiary, Laclede Gas, Missouri's largest natural gas distribution company. Laclede Gas is regulated by the MoPSC and serves the City of St. Louis and parts of ten counties in eastern Missouri. Laclede Gas delivers natural gas to retail customers at rates and in accordance with tariffs authorized by the MoPSC. The Utility's earnings are primarily generated by the sale of heating energy. The Utility's weather mitigation rate design lessens the impact of weather volatility on Laclede Gas' customers during cold winters and stabilizes the Utility's earnings by recovering

fixed costs more evenly during the heating season. Due to the seasonal nature of the business of Laclede Gas, Laclede Group's earnings are typically concentrated in the November through April period, which generally corresponds with the heating season.

Laclede Energy Resources, Inc. (LER), which includes its wholly owned subsidiary LER Storage Services, Inc. (LSS), is engaged in the marketing of natural gas and related activities on a non-regulated basis and is reported in the Gas Marketing segment. LER markets natural gas to both on-system Utility transportation customers and customers outside of Laclede Gas' traditional service territory, including large retail and wholesale customers. LER's operations and customer base are more subject to fluctuations in market conditions than the Utility. LSS has contracted storage capacity for 1 Bcf of natural gas through January 2014. Further, and separately, LSS has entered into a precedent agreement with a natural gas storage facility operator that will provide 1 Bcf of natural gas storage subject to the facility's successful completion of an expansion program in mid-2013.

Other subsidiaries provide less than 10% of consolidated revenues.

Based on the nature of the business of the Company and its subsidiaries, as well as current economic conditions, management focuses on the following key variables in evaluating the financial condition and results of operations and managing the business:

Gas Utility Segment:

- the Utility's ability to recover the costs of purchasing and distributing natural gas from its customers;
- the impact of weather and other factors, such as customer conservation, on revenues and expenses;
- changes in the regulatory environment at the federal, state, and local levels, as well as decisions by regulators, that impact the Utility's ability to earn its authorized rate of return;
- the Utility's ability to access credit markets and maintain working capital sufficient to meet operating requirements; and,
- the effect of natural gas price volatility on the business.

Gas Marketing Segment:

- the risks of competition;
- fluctuations in natural gas prices;
- new national pipeline infrastructure projects;
- the ability to procure firm transportation and storage services at reasonable rates;
- credit and/or capital market access;
- counterparty risks;
- the effect of natural gas price volatility on the business; and,
- additional growth.

Further information regarding how management seeks to manage these key variables is discussed below.

Laclede Gas continues to provide reliable natural gas service at a reasonable cost, while maintaining and building a secure and dependable infrastructure. The Utility's strategy focuses on improving performance and mitigating the impact of weather fluctuations on Laclede Gas' customers while improving the ability to recover its authorized distribution costs and rate of return. The Utility's distribution costs are the essential, primarily fixed, expenditures it must incur to operate and maintain more than 16,000 miles of mains and services comprising its natural gas distribution system and related storage facilities. The Utility's distribution costs include wages and employee benefit costs, depreciation and maintenance expenses, and other regulated utility operating expenses, excluding natural and propane gas expense. Distribution costs are considered in the ratemaking process, and recovery of these types of costs is included in revenues generated through the Utility's tariff rates, as approved by the MoPSC. The settlement of the Utility's rate case in 2010 retained the Utility's weather mitigation rate design that better ensures the recovery of its fixed costs and margins despite variations in sales volumes due to the impacts of weather and other factors that affect customer usage.

The Utility's income from off-system sales and capacity release remains subject to fluctuations in market conditions. The Utility is allowed to retain 15% to 25% of the first \$6 million in annual income earned (depending on the level of income earned) and 30% of income exceeding \$6 million annually. Some of the factors impacting the level of off-system sales include the availability and cost of the Utility's natural gas supply, the weather in its service area, and the weather in other markets. When Laclede Gas' service area experiences warmer-than-normal weather while other markets experience colder weather or supply constraints, some of the Utility's natural gas supply is available for off-system sales and there may be a demand for such supply in other markets. See the Regulatory and Other Matters section on page 36 of this report for additional information on regulatory issues relative to the Utility.

Laclede Gas works actively to reduce the impact of wholesale natural gas price volatility on its costs by strategically structuring its natural gas supply portfolio to increase its gas supply availability and pricing alternatives and through the use of derivative instruments to protect its customers from significant changes in the commodity price of natural gas. Nevertheless, the overall cost of purchased gas remains subject to fluctuations in market conditions. The Utility's Purchased Gas Adjustment (PGA) Clause allows Laclede Gas to flow through to customers, subject to prudence review by the MoPSC, the cost of purchased gas supplies, including costs, cost reductions, and related carrying costs associated with the use of derivative instruments to hedge the purchase price of natural gas, as well as gas inventory carrying costs. The Utility believes it will continue to be able to obtain sufficient gas supply. The price of natural gas supplies and other economic conditions may affect sales volumes, due to the conservation efforts of customers, and cash flows associated with the timing of collection of gas costs and related accounts receivable from customers.

The Utility relies on both short-term credit and long-term capital markets, as well as cash flows from operations, to satisfy its seasonal cash requirements and fund its cost of capital expenditures. Laclede Gas' ability to issue commercial paper supported by lines of credit, to issue long-term bonds, or to obtain new lines of credit is dependent on current conditions in the credit and capital markets. Management focuses on maintaining a strong balance sheet and believes it currently has adequate access to credit and capital markets and will have sufficient capital resources to meet its foreseeable obligations. See the Liquidity and Capital Resources section on page 38 for additional information.

LER provides both on-system Utility transportation customers and customers outside of Laclede Gas' traditional service area with another choice in non-regulated natural gas suppliers. LER utilizes its natural gas supply agreements, transportation agreements, park and loan agreements, storage agreements, and other executory contracts to support a variety of services to its customers at competitive prices. It closely monitors and manages the natural gas commodity price and volatility risks associated with providing such services to its customers through the use of a variety of risk management activities, including the use of exchange-traded/cleared derivative instruments and other contractual arrangements. LER is committed to managing commodity price risk, while it seeks to expand the services that it now provides. Nevertheless, income from LER's operations is more subject to fluctuations in market conditions than the Utility's operations. LER's business is directly impacted by the effects of competition in the marketplace, the impacts of new pipeline infrastructure and surplus natural gas supplies on natural gas commodity prices. Further, LER's profitability will likely be impacted by the effects of the expiration of certain of its natural gas supply and transportation agreements if those contracts cannot be replaced and/or renewed with arrangements with similar terms and pricing.

In addition to its operating cash flows, LER relies on Laclede Group's parental guarantees to secure its purchase and sales obligations of natural gas. LER also has access to Laclede Group's liquidity resources. A large portion of LER's receivables are from customers in the energy industry. LER also enters into netting arrangements with many of its energy counterparties to reduce overall credit and collateral exposure. Although LER's uncollectible amounts are closely monitored and have not been significant, increases in uncollectible amounts from customers are possible and could adversely affect LER's liquidity and results.

LER carefully monitors the creditworthiness of counterparties to its transactions. LER performs in-house credit reviews of potential customers and may require credit assurances such as prepayments, letters of credit, or parental guarantees when appropriate. Credit limits for customers are established and monitored.

In response to new pipeline infrastructure and more abundant natural gas supplies, LER may have the opportunity to enter into subsequent offsetting purchase or sale transactions at the same location in order to satisfy its commitments without incurring fuel cost to transport natural gas to a different location. Thus, LER cannot be certain that all of its wholesale purchase and sale transactions will settle physically. As such, certain transactions entered into on or after January 1, 2012 are designated as trading activities for financial reporting purposes, due to their settlement characteristics, rather than elected for normal purchases or normal sales designations under generally accepted

accounting principles (GAAP). Results of operations from trading activities are reported on a net basis (instead of a gross basis) in Gas Marketing Operating Revenues, which may cause reductions in and/or volatility in the Company's operating revenues, but has no effect on operating income or net income.

In the course of its business, LER enters into commitments associated with the purchase or sale of natural gas. In accordance with GAAP, some of LER's purchase and sale transactions are not recognized in earnings until the natural gas is physically delivered, while other energy-related transactions, including those designated as trading activities, are required to be accounted for as derivatives, with the changes in their fair value (representing unrealized gains or losses) recorded in earnings in periods prior to settlement. Because related transactions of a purchase and sale strategy may be accounted for differently, there may be timing differences in the recognition of earnings under GAAP and economic earnings realized upon settlement. The Company reports both GAAP and net economic earnings (non-GAAP), as discussed below.

EARNINGS

The Laclede Group reports net income and earnings per share determined in accordance with GAAP. Management also uses the non-GAAP measures of net economic earnings and net economic earnings per share when internally evaluating results of operations. These non-GAAP measures exclude from net income the after-tax impacts of fair value accounting and timing adjustments associated with energy-related transactions. These adjustments include timing differences where the accounting treatment differs from the economic substance of the underlying transaction, including the following:

- Net unrealized gains and losses on energy-related derivatives that are required by GAAP fair value accounting associated with current changes in the fair value of financial and physical transactions prior to their completion and settlement. These unrealized gains and losses result primarily from two sources:
 - 1) changes in the fair values of physical and/or financial derivatives prior to the period of settlement; and, ineffective portions of accounting hedges, required to be recorded in earnings prior to settlement, due to differences
 - 2) in commodity price changes between the locations of the forecasted physical purchase or sale transactions and the locations of the underlying hedge instruments;
- Lower of cost or market adjustments to the carrying value of commodity inventories resulting when the market price of the commodity falls below its original cost, to the extent that those commodities are economically hedged; and
- Realized gains and losses resulting from the settlement of economic hedges prior to the sale of the physical commodity.

These adjustments eliminate the impact of timing differences and the impact of current changes in the fair value of financial and physical transactions prior to their completion and settlement. Unrealized gains or losses are recorded in each period until being replaced with the actual gains or losses realized when the associated physical transaction(s) occur. While management uses these non-GAAP measures to evaluate both Laclede Gas and LER, the net effect of adjustments on the Utility's earnings is minimal because gains or losses on its natural gas derivative instruments are deferred pursuant to its PGA Clause, as authorized by the MoPSC.

Management believes that excluding the earnings volatility caused by recognizing changes in fair value prior to settlement and other timing differences associated with related purchase and sale transactions provides a useful representation of the economic effects of only the actual settled transactions and their effects on results of operations. In addition, management excludes the effect of costs related to unique acquisition, divestiture, and restructuring activities, when evaluating on-going performance, and therefore excludes these costs from net economic earnings. These internal non-GAAP operating metrics should not be considered as an alternative to, or more meaningful than, GAAP measures such as net income. Reconciliations of net economic earnings and net economic earnings per share to the Company's most directly comparable GAAP measures are provided below.

Quarter Ended March 31, 2013

Reconciliation of Consolidated Net Economic Earnings (Non-GAAP) to Consolidated Net Income (GAAP)

(Millions, except per share amounts)	Gas Utility	Gas Marketing	Unallocated & Other	Total	Per Share Amounts**
Quarter Ended March 31, 2013					
Net Economic Earnings (Losses) (Non-GAAP)	\$30.2	\$2.4	\$(0.1)	\$32.5	\$1.44
Add: Unrealized gain (loss) on energy-related derivatives*	—	(0.6)	—	(0.6)	(0.03)
Add: Acquisition, divestiture and restructuring activities*	—	—	(1.7)	(1.7)	(0.07)
Net Income (Loss) (GAAP)	\$30.2	\$1.8	\$(1.8)	\$30.2	\$1.34
Quarter Ended March 31, 2012					
Net Economic Earnings (Losses) (Non-GAAP)	\$25.8	\$2.5	\$0.1	\$28.4	\$1.27
Add: Unrealized gain (loss) on energy-related derivatives*	—	2.0	—	2.0	0.09
Add: Lower of cost or market inventory adjustments*	—	(0.6)	—	(0.6)	(0.03)
Add: Realized gain (loss) on economic hedges prior to the sale of the physical commodity*	—	(0.1)	—	(0.1)	(0.01)
Add: Acquisition, divestiture and restructuring activities*	—	—	—	—	—
Net Income (Loss) (GAAP)	\$25.8	\$3.8	\$0.1	\$29.7	\$1.32

Amounts presented net of income taxes. Income taxes are calculated by applying federal, state, and local income tax rates applicable to ordinary income to the amounts of the pre-tax reconciling items. For the quarters ended March 31, 2013 and 2012, the total net amount of income tax (benefit) expense included in the reconciling items above is (\$1.4) million and \$0.8 million, respectively.

** Net economic earnings per share is calculated by replacing consolidated net income with consolidated net economic earnings in the GAAP diluted earnings per share calculation.

Laclede Group's net income was \$30.2 million for the quarter ended March 31, 2013, compared with \$29.7 million for the quarter ended March 31, 2012. Basic and diluted earnings per share for the quarter ended March 31, 2013 were \$1.34, compared with basic and diluted earnings per share of \$1.33 and \$1.32, respectively, for the quarter ended March 31, 2012. Earnings increased compared to last year primarily due to improved results reported by Laclede Group's Gas Utility Segment. These factors were partially offset by lower net income reported by the Gas Marketing Segment and acquisition costs incurred this quarter totaling \$1.7 million, net of tax, or \$0.07 per share, associated with agreements to acquire certain assets and liabilities from SUG, as described previously. Acquisition-related costs, among other items, are excluded from net economic earnings, which were \$32.5 million for the quarter ended March 31, 2013, compared with \$28.4 million for the same quarter last year. Net economic earnings per share were \$1.44 for the quarter ended March 31, 2013, compared with \$1.27 for the quarter ended March 31, 2012.

Gas Utility net income and net economic earnings both increased by \$4.4 million for the quarter ended March 31, 2013, compared with the quarter ended March 31, 2012. The increase was primarily due to the following factors, quantified on a pre-tax basis:

- increased sales margins reflecting colder weather this year totaling \$4.4 million;
- decreases in employee benefit expenses of \$2.8 million; and
- higher Infrastructure System Replacement Surcharge (ISRS) revenues totaling \$1.1 million.

These benefits were partially offset by higher depreciation and amortization expenses totaling \$1.1 million.

The Gas Marketing segment reported GAAP earnings totaling \$1.8 million, a decrease of \$2.0 million compared with the same quarter last year. Net economic earnings for the quarter ended March 31, 2013 decreased \$0.1 million from the quarter ended March 31, 2012. The decrease in net economic earnings was primarily attributable to reduced sales margins, reflecting low price volatility and basis differentials in the current natural gas market and the expiration of a favorable supply contract, largely offset by higher transaction volumes and the realization of seasonal storage spreads. On a GAAP basis, LER's results were further impacted by the effect of higher net unrealized losses from certain of LER's energy-related derivative contracts.

Other net income and net economic earnings decreased \$1.9 million and \$0.2 million, respectively, compared with the same period last year. The decrease in net income is primarily due to unallocated expenses during the quarter ended March 31, 2013, attributable to the pending acquisition of MGE and NEG from SUG totaling \$1.7 million, net of tax.

Gas Utility Operating Revenues

Laclede Gas passes on to Utility customers (subject to prudence review by the MoPSC) increases and decreases in the wholesale cost of natural gas in accordance with its PGA Clause. The volatility of the wholesale natural gas market results in fluctuations from period to period in the recorded levels of, among other items, revenues and natural gas cost expense. Nevertheless, increases and decreases in the cost of gas associated with system gas sales volumes have no direct effect on net revenues and net income.

Gas Utility Operating Revenues for the quarter ended March 31, 2013 were \$354.1 million, or \$55.5 million more than the same period last year. Temperatures experienced in the Utility's service area during the quarter ended March 31, 2013 were 45.7% colder than the same quarter last year and 3.5% colder than normal. Last year's temperatures were the warmest on record. Total system therms sold and transported were 413.0 million for the quarter ended March 31, 2013, compared with 305.2 million for the same period last year. Total off-system therms sold and transported were 102.0 million for the quarter ended March 31, 2013, compared with 130.0 million for the same period last year. The increase in Gas Utility Operating Revenues was primarily attributable to the following factors:

(Millions)

Higher system sales volumes and other variations	\$60.2	
Higher prices charged for off-system sales	10.9	
Lower wholesale gas costs passed on to Utility customers (subject to prudence review by the MoPSC)	(9.4)	)
Lower off-system sales volumes (reflecting less favorable market conditions as described in greater detail in the Results of Operations - Overview)	(7.3)	)
Higher ISRS revenues	1.1	
Total Variation	\$55.5	

Gas Utility Operating Expenses

Gas Utility Operating Expenses for the quarter ended March 31, 2013 increased \$59.4 million from the same quarter last year. Natural and propane gas expense increased \$59.3 million, or 34.6%, from last year's level, primarily attributable to increased system volumes purchased for sendout and higher off-system gas expense, partially offset by lower rates charged by our suppliers. Other operation and maintenance expense decreased \$2.6 million, or 6.0%, primarily due to lower employee benefit expenses, a lower provision for uncollectible accounts, a higher rate of overheads capitalized, and reduced customer accounts expenses, partially offset by increased charges for outside services. Depreciation and amortization expense increased \$1.1 million primarily due to additional depreciable property. Taxes, other than income taxes, increased \$1.7 million, or 8.3%, primarily due to increased gross receipts taxes (attributable to increased system sales revenues).

Gas Marketing Operating Revenues and Operating Expenses

Gas Marketing Operating Revenues and Operating Expenses decreased \$18.2 million and \$25.8 million, respectively, primarily due to the effect of recording certain transactions on a net basis (instead of a gross basis) which had no effect on earnings, as described in greater detail in Results of Operations – Overview. The decreases were partially offset by higher volumes purchased and sold as well as higher per unit gas prices.

Other Operating Revenues and Operating Expenses

Other Operating Revenues increased by \$2.1 million, primarily due to a sale of propane inventory by Laclede Pipeline Company during the quarter ended March 31, 2013. The increase in Other Operating Expenses, totaling \$4.6 million, was primarily due to the acquisition expenses discussed above and expenses associated with the aforementioned propane sale. Additional acquisition expenses are expected to be incurred prior to the closing of the Transaction.

Interest Charges

Interest charges during the quarter ended March 31, 2013 increased \$0.4 million from the same period last year primarily due to expenses associated with the Company's bridge loan facility, partially offset by lower interest on long-term debt. The slightly lower interest on long-term debt reflects the net effect of the October 2012 maturity of \$25 million of 6 1/2% first mortgage bonds and the December 2012 and March 2013 issuances of additional long-term debt of \$25 million and \$100 million, respectively. Average short-term interest rates were 0.3% for both the quarters ended March 31, 2013 and 2012. Average short-term borrowings were \$46.7 million for the quarter ended March 31, 2013, compared with \$68.7 million for the quarter ended March 31, 2012.

Six Months Ended March 31, 2013

Reconciliation of Consolidated Net Economic Earnings (Non-GAAP) to Consolidated Net Income (GAAP)

(Millions, except per share amounts)	Gas Utility	Gas Marketing	Unallocated & Other	Total	Per Share Amounts**
Six Months Ended March 31, 2013					
Net Economic Earnings (Losses) (Non-GAAP)	\$55.5	\$5.6	\$(0.4)	\$60.7	\$2.69
Add: Unrealized gain (loss) on energy-related derivatives*	(0.1)	(0.9)	—	(1.0)	(0.05)
Add: Acquisition, divestiture and restructuring activities*	—	—	(3.9)	(3.9)	(0.17)
Net Income (Loss) (GAAP)	\$55.4	\$4.7	\$(4.3)	\$55.8	\$2.47
Six Months Ended March 31, 2012					
Net Economic Earnings (Losses) (Non-GAAP)	\$46.8	\$6.0	\$0.5	\$53.3	\$2.38
Add: Unrealized gain (loss) on energy-related derivatives*	0.1	2.2	—	2.3	0.11
Add: Lower of cost or market inventory adjustments*	—	(0.6)	—	(0.6)	(0.03)
Add: Realized gain (loss) on economic hedges prior to the sale of the physical commodity*	—	(0.1)	—	(0.1)	(0.01)
Net Income (Loss) (GAAP)	\$46.9	\$7.5	\$0.5	\$54.9	\$2.45

Amounts presented net of income taxes. Income taxes are calculated by applying federal, state, and local income tax rates applicable to ordinary income to the amounts of the pre-tax reconciling items. For the six months ended March 31, 2013 and 2012, the total net amount of income tax (benefit) expense included in the reconciling items above is (\$3.0) million and \$1.0 million, respectively.

** Net economic earnings per share is calculated by replacing consolidated net income with consolidated net economic earnings in the GAAP diluted earnings per share calculation.

Laclede Group's net income was \$55.8 million for the six months ended March 31, 2013, compared with \$54.9 million for the six months ended March 31, 2012. Basic and diluted earnings per share for the six months March 31, 2013 were \$2.48 and \$2.47, respectively, compared with basic and diluted earnings per share of \$2.45 for the six months ended March 31, 2012. Earnings increased compared to last year primarily due to improved results reported by Laclede Group's Gas Utility Segment, partially offset by acquisition costs incurred during the period totaling \$3.9 million, net of tax, or \$0.17 per share, associated with agreements to acquire certain assets and liabilities from SUG, as described previously. Additionally, earnings were impacted by decreased income from the Gas Marketing Segment. Acquisition-related costs, among other items, are excluded from net economic earnings, which were \$60.7 million for the six months ended March 31, 2013, compared with \$53.3 million for the same period last year. Net economic earnings per share were \$2.69 for the six months ended March 31, 2013, compared with \$2.38 for the six months ended March 31, 2012.

Gas Utility net income and net economic earnings increased by \$8.5 million and \$8.7 million, respectively for the six months ended March 31, 2013, compared with the six months ended March 31, 2012. The increase was primarily due to the following factors, quantified on a pre-tax basis:

- increased sales margins reflecting colder weather this year totaling \$5.4 million;
- decreases in employee benefit expenses totaling \$3.0 million;
- a lower provision for uncollectible accounts totaling \$2.9 million; and
- higher ISRS revenues totaling \$2.4 million.

These benefits were partially offset by higher depreciation and amortization expenses totaling \$2.0 million.

The Gas Marketing segment reported GAAP earnings totaling \$4.7 million, a decrease of \$2.8 million compared with the same period last year. Net economic earnings for the six months ended March 31, 2013 decreased \$0.4 million from the six months ended March 31, 2012. The decrease in net economic earnings was primarily attributable to reduced sales margins, reflecting current market conditions and the expiration of a favorable supply contract, largely offset by higher transaction volumes. On a GAAP basis, LER's results were further impacted by the effect of higher net unrealized losses from certain of LER's energy-related derivative contracts.

Other net income and net economic earnings decreased \$4.8 million and \$0.9 million, respectively, compared with the same period last year. The decrease in net income is primarily due to unallocated expenses during the six months ended March 31, 2013, attributable to the pending acquisition of MGE and NEG from SUG totaling \$3.9 million, net of tax.

Gas Utility Operating Revenues

Laclede Gas passes on to Utility customers (subject to prudence review by the MoPSC) increases and decreases in the wholesale cost of natural gas in accordance with its PGA Clause. The volatility of the wholesale natural gas market results in fluctuations from period to period in the recorded levels of, among other items, revenues and natural gas cost expense. Nevertheless, increases and decreases in the cost of gas associated with system gas sales volumes have no direct effect on net revenues and net income.

Gas Utility Operating Revenues for the six months ended March 31, 2013 were \$604.2 million, or \$54.7 million more than the same period last year. Temperatures experienced in the Utility's service area during the six months ended March 31, 2013 were 32.6% colder than the same period last year, but 1.6% warmer than normal. Last year's temperatures were the warmest on record. Total system therms sold and transported were 674.1 million for the six months ended March 31, 2013, compared with 543.7 million for the same period last year. Total off-system therms sold and transported were 182.4 million for the six months ended March 31, 2013, compared with 228.2 million for the same period last year. The increase in Gas Utility Operating Revenues was primarily attributable to the following factors:

(Millions)

Higher system sales volumes and other variations	\$74.2	
Lower wholesale gas costs passed on to Utility customers (subject to prudence review by the MoPSC)	(21.0)	)
Lower off-system sales volumes (reflecting less favorable market conditions as described in greater detail in the Results of Operations - Overview)	(13.5)	)
Higher prices charged for off-system sales	12.6	
Higher ISRS revenues	2.4	
Total Variation	\$54.7	

Gas Utility Operating Expenses

Gas Utility Operating Expenses for the six months ended March 31, 2013 increased \$47.0 million from the same period last year. Natural and propane gas expense increased \$49.0 million, or 15.4%, from last year's level, primarily attributable to increased system volumes purchased for sendout and higher off-system gas expense, partially offset by lower rates charged by our suppliers. Other operation and maintenance expenses decreased \$5.8 million, or 6.7%, primarily due to lower employee benefit expenses, a lower provision for uncollectible accounts, a higher rate of overheads capitalized, and reduced customer accounts expenses, partially offset by increased charges for outside services. Depreciation and amortization expense increased \$2.0 million primarily due to additional depreciable property. Taxes, other than income taxes, increased \$1.8 million, or 5.2%, primarily due to increased gross receipts taxes (attributable to increased system sales revenues).

Gas Marketing Operating Revenues and Operating Expenses

Gas Marketing Operating Revenues and Operating Expenses decreased \$121.5 million and \$121.0 million, respectively, primarily due to the effect of recording certain transactions on a net basis (instead of a gross basis) which had no effect on earnings, as described in greater detail in Results of Operations – Overview. The decreases were partially offset by higher volumes purchased and sold and, to a lesser extent, higher per unit gas prices.

Other Operating Revenues and Operating Expenses

Other Operating Revenues increased by \$2.4 million, primarily due to a sale of propane inventory by Laclede Pipeline Company during the six months ended March 31, 2013. The increase in Other Operating Expenses, totaling \$9.3 million, was primarily due to the acquisition-related expenses discussed above and expenses associated with the aforementioned propane sale. Additional acquisition expenses are expected to be incurred prior to the closing of the Transaction.

Other Income and (Income Deductions) - Net

Other Income and (Income Deductions) - Net decreased \$0.9 million primarily due to lower net investment gains.

Interest Charges

Interest charges during the six months ended March 31, 2013 increased \$0.1 million from the same period last year primarily due expenses associated with the Company's bridge loan facility, partially offset by lower interest on long-term debt. The lower interest on long-term debt reflects the net effect of the October 2012 maturity of \$25 million of 6 1/2% first mortgage bonds and the December 2012 and March 2013 issuances of additional long-term debt of \$25 million and \$100 million, respectively. Average short-term interest rates were 0.3% for both the six months ended March 31, 2013 and 2012. Average short-term borrowings were \$61.0 million for the six months ended March 31, 2013, compared with \$75.0 million for the six months ended March 31, 2012.

Income Taxes

The \$1.7 million decrease in income taxes was primarily due to lower pre-tax income and various property-related deductions.

REGULATORY AND OTHER MATTERS

The MoPSC Staff previously proposed disallowances related to Laclede Gas' recovery of its purchased gas costs totaling \$6.0 million pertaining to Laclede Gas' purchase of gas from a marketing affiliate, LER, applicable to fiscal years 2005 through 2007. The MoPSC Staff also proposed a number of non-monetary recommendations, based on its review of gas costs for fiscal years 2008 through 2011. Laclede Gas believes that the proposed disallowances lack merit and is vigorously opposing these adjustments. Management, after discussion with counsel, continues to believe the final outcome of these matters will not have a material effect on the Company's financial position, results of operations, or cash flows. Laclede Gas is currently in discussions with the MoPSC Staff and other parties to resolve these matters.

In connection with its review of these affiliate transactions, Laclede Gas objected, on the grounds of relevance, to MoSPC data requests seeking to obtain from LER certain of LER's proprietary documents unrelated to Laclede Gas' purchases from LER. On July 7, 2010, the MoPSC Staff filed a complaint against Laclede Gas alleging that, by stating that it was not in possession of proprietary LER documents, Laclede Gas violated the MoPSC Order authorizing the holding company structure (2001 Order). Laclede Gas counterclaimed stating the Staff failed to adhere to pricing

provisions of the MoPSC's affiliate transaction rules and Laclede Gas' Cost Allocation Manual. By orders dated November 3, 2010 and February 4, 2011, respectively, the MoPSC dismissed Laclede's counterclaim and granted summary judgment to Staff, finding that Laclede Gas violated the terms of the 2001 Order and authorizing its General Counsel to seek penalties in court against Laclede Gas. These Orders were later reversed by the Cole County Circuit Court, but ultimately upheld by the Western District Court of Appeals. On March 19, 2013, the Missouri Supreme Court declined Laclede Gas' request to review the opinion of the Western District Court of Appeals relating to the information-related requirements of the 2001 Order. As a result, additional LER documentation may need to be shared with the MoPSC staff. In addition, certain related complaints filed by the MoPSC Staff on October 6, 2010 and a counterclaim by Laclede Gas against Staff are still pending before the Commission. Management, after discussion with counsel, continues to believe the final outcome of these matters will not have a material effect on the Company's financial position, results of operations, or cash flows. Laclede Gas is currently in discussions with the MoPSC Staff and other parties to resolve these above matters.

On December 21, 2012, Laclede Gas filed tariff sheets in a new general rate case proceeding that are designed to increase the Utility's total revenues by \$43.6 million, net of current annualized ISRS revenues. On December 27, 2012, the MoPSC suspended implementation of the Utility's proposed rates and set the case for hearing in August 2013.

On January 14, 2013, the Company filed an application with the MoPSC for approval to acquire the assets of MGE from SUG as reported in the Acquisition Agreements section on page 28. A similar filing was made with the Massachusetts Department of Public Utilities (MDPU) on January 24, 2013 for approval of the acquisition of NEG. On March 15, 2013, the MDPU issued a procedural schedule setting the case for hearing during the last week in June 2013.

Also on January 14, 2013, the Utility made an ISRS filing with the Commission and an increase of \$4.8 million was approved by the MoPSC effective March 15, 2013.

On June 29, 2010, the Office of Federal Contract Compliance Programs issued a Notice of Violations to Laclede Gas alleging lapses in certain employment selection procedures during a two-year period ending in February 2006. The Company believes that the allegations lack merit and is vigorously defending its position. Management, after discussion with counsel, believes that the final outcome of these matters will not have a material effect on the consolidated financial position and results of operations, or cash flows of the Company.

CRITICAL ACCOUNTING POLICIES

Our discussion and analysis of our financial condition, results of operations, liquidity, and capital resources is based upon our consolidated financial statements, which have been prepared in accordance with GAAP. GAAP requires that we make estimates and judgments that affect the reported amounts of assets, liabilities, revenues and expenses, and related disclosure of contingent assets and liabilities. We evaluate our estimates on an ongoing basis. We base our estimates on historical experience and on various other assumptions that we believe are reasonable under the circumstances, the results of which form the basis for making judgments about the carrying values of assets and liabilities that are not readily apparent from other sources. Actual results may differ from these estimates. Our critical accounting policies used in the preparation of our Consolidated Financial Statements are described in Item 7 of our Annual Report on Form 10-K for the fiscal year ended September 30, 2012 and include the following:

- ▲Accounts receivable and allowance for doubtful accounts
- ◆Employee benefits and postretirement obligations
- ◆Regulated operations
- ◆Non-Regulated Gas Marketing Energy Contracts

There were no significant changes to these critical accounting policies during the six months ended March 31, 2013.

For discussion of other significant accounting policies, see Note 1 of the Notes to Consolidated Financial Statements included in the Company's Form 10-K for the fiscal year ended September 30, 2012.

ACCOUNTING PRONOUNCEMENTS

The Company has evaluated or is in the process of evaluating the impact that recently issued accounting standards will have on the Company's financial position or results of operations upon adoption. For disclosures related to the adoption of new accounting standards, see the New Accounting Standards section of Note 1 of the Notes to Consolidated Financial Statements.

The Company continues to monitor the developments of the Financial Accounting Standards Board (FASB) relative to possible changes in accounting standards. Currently, the FASB is considering various changes to U. S. GAAP, some of which may be significant, as part of a joint effort with the International Accounting Standards Board to converge accounting standards.

Future developments, depending on the outcome, have the potential to impact the Company's financial condition and results of operations.

FINANCIAL CONDITION

CASH FLOWS

The Company's short-term borrowing requirements typically peak during colder months when Laclede Gas borrows money to cover the lag between when it purchases its natural gas and when its customers pay for that gas. Changes in the wholesale cost of natural gas (including cash payments for margin deposits associated with the Utility's use of natural gas derivative instruments), variations in the timing of collections of gas cost under the Utility's PGA Clause, the seasonality of accounts receivable balances, and the utilization of storage gas inventories cause short-term cash requirements to vary during the year and from year to year, and can cause significant variations in the Utility's cash provided by or used in operating activities.

Net cash provided by operating activities was \$142.4 million for the six months ended March 31, 2013, compared with \$71.5 million for the same period last year. The variation is primarily associated with the timing of collections of gas cost under the Utility's PGA Clause, primarily due to reduced cash payments for margin deposits associated with the Utility's use of natural gas derivative instruments. The variation also reflects decreased cash payments for the funding of pension plans. These benefits were partially offset by changes in delayed and advance customer billings.

Net cash used in investing activities for the six months ended March 31, 2013 was \$64.8 million, compared with \$42.1 million for the six months ended March 31, 2012. The variation primarily reflects additional capital expenditures this year for distribution plant and information technology investments.

Net cash provided by financing activities was \$41.9 million for the six months ended March 31, 2013, compared with net cash used in financing activities of \$63.3 million for the six months ended March 31, 2012. The variation primarily reflects the issuance of additional long-term debt this year, partially offset by the maturity of long-term debt.

LIQUIDITY AND CAPITAL RESOURCES

Cash and Cash Equivalents

Laclede Group had temporary cash investments totaling \$131.3 million at March 31, 2013, earning an average interest rate of 0.1%. This includes \$35.5 million held by Laclede Gas, also at an average interest rate of 0.1%. These investments, which are presented in the Cash and cash equivalents line of the Consolidated Balance Sheets, were diversified among money market funds and interest-bearing deposits at highly-rated commercial banks. The money market funds are accessible by the Company on demand. The bank deposits are also generally available on demand, though the banks reserve the right to require seven days' notice for a withdrawal. These funds are used to support the working capital needs of the Company's subsidiaries. The balance of short-term investments ranged between \$10.4 million and \$131.3 million during the six months ended March 31, 2013. Due to lower yields available to Laclede Group on its short-term investments, Laclede Group elected to provide a portion of Laclede Gas' short-term funding through intercompany lending during the six months ended March 31, 2013, but there were no such borrowings at March 31, 2013.

Short-term Debt

As indicated in the discussion of cash flows above, the Company's short-term borrowing requirements typically peak during the colder months. These short-term cash requirements can be met through the sale of commercial paper supported by lines of credit with banks or through direct use of the lines of credit. At March 31, 2013, Laclede Gas had a syndicated line of credit in place of \$300 million from seven banks, \$257.1 million of which is scheduled to

expire in July 2017 and \$42.9 million of which is scheduled to expire in July 2016. The largest portion provided by a single bank is 17.9%. Laclede Gas' line of credit includes a covenant limiting total debt, including short-term debt, to no more than 70% of total capitalization. As a result of certain amendments made on January 16, 2013, this maximum percentage will temporarily increase to 72.5% if the MGE acquisition is consummated. Such temporary increase would be effective from the date of consummation through September 30, 2014. As defined in the line of credit, total debt was 45% of total capitalization on March 31, 2013.

Short-term cash requirements outside of Laclede Gas have generally been met with internally generated funds. However, Laclede Group has \$50 million in a syndicated line of credit, \$42.9 million of which expires in July 2017 and \$7.1 million of which expires in July 2016, to meet short-term liquidity needs of its subsidiaries. The line of credit has a covenant limiting the total debt of the consolidated Laclede Group to no more than 70% of the Company's total capitalization. As a result of certain amendments made on January 16, 2013, this maximum percentage will temporarily increase to 72.5% if the MGE acquisition is consummated. Such temporary increase would be effective from the date of consummation through September 30, 2014. As defined in the line of credit, this ratio stood at 42% on March 31, 2013. Occasionally, Laclede Group's lines may be used to provide for the funding needs of various subsidiaries. There were no borrowings under Laclede Group's lines during the six months ended March 31, 2013.

Information about Laclede Group's consolidated short-term borrowings (excluding intercompany borrowings) during the six months ended March 31, 2013 and as of March 31, 2013, is presented below:

Six Months Ended March 31, 2013	Commercial Paper Borrowings
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