

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

FORM 10-Q

[ X ] QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15 (d) OF THE  
SECURITIES EXCHANGE ACT OF 1934

For the quarterly period ended June 30, 1996  
-----

Commission file number 1-1402  
-----

SOUTHERN CALIFORNIA GAS COMPANY

-----  
(Exact name of registrant as specified in its charter)

California

95-1240705

-----  
(State or other jurisdiction of incorporation or organization) (I.R.S. Employer Identification No.)

555 West Fifth Street, Los Angeles, California 90013-1011  
-----

(Address of principal executive offices)  
(Zip Code)

(213) 244-1200

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

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

Yes X No  
---

The number of shares of common stock outstanding on June 30, 1996 was 91,300,000.

PART I - FINANCIAL INFORMATION

ITEM 1. FINANCIAL STATEMENTS.

SOUTHERN CALIFORNIA GAS COMPANY AND SUBSIDIARY  
CONDENSED STATEMENT OF CONSOLIDATED INCOME  
(Thousands of Dollars)

	Three Months Ended June 30		Six Months Ended June 30	
	1996	1995	1996	1995
	-----			
	(Unaudited)			
Operating Revenues	\$497,100	\$579,559	\$1,116,940	\$1,184,249
	-----			
Operating Expenses:				
Cost of gas distributed	143,683	182,155	393,650	413,845
Operation and maintenance	190,575	204,797	347,348	374,338
Depreciation	62,771	59,348	123,098	118,326
Income taxes	26,457	39,029	70,823	79,964
Other taxes and franchise payments	19,522	20,350	48,988	50,624
	-----			
Total	443,008	505,679	983,907	1,037,097
	-----			
Net Operating Revenue	54,092	73,880	133,033	147,152
	-----			
Other Income and (Deductions):				
Interest income	488	3,223	806	4,820
Regulatory interest	176	(55)	728	1,582
Allowance for equity funds used during construction	1,022	504	2,722	1,139
Income taxes on non-operating income	(93)	(477)	(112)	(293)
Other - net	(2,663)	(1,309)	(4,181)	(3,043)
	-----			
Total	(1,070)	1,886	(37)	4,205
	-----			
Interest Charges and (Credits):				
Interest on long-term debt	19,691	22,195	40,242	44,451
Other interest	1,840	837	5,255	3,490
Allowance for borrowed funds used during construction	(585)	(291)	(1,563)	(658)
	-----			
Total	20,946	22,741	43,934	47,283
	-----			
Net Income	32,076	53,025	89,062	104,074
Dividends on Preferred Stock	1,868	2,918	4,675	5,846
	-----			
Net Income Applicable to Common Stock	\$ 30,208	\$ 50,107	\$ 84,387	\$ 98,228
	=====			

See Notes to Condensed Consolidated Financial Statements.

SOUTHERN CALIFORNIA GAS COMPANY AND SUBSIDIARY  
 CONDENSED CONSOLIDATED BALANCE SHEET  
 ASSETS  
 (Thousands of Dollars)

	June 30 1996 ----- (Unaudited)	December 31 1995 -----
Utility Plant	\$5,883,516	\$5,807,940
Less accumulated depreciation	2,705,505	2,594,713
	-----	-----
Utility plant - net	3,178,011	3,213,227
	-----	-----
Current Assets:		
Cash and cash equivalents	6	12,611
Accounts and notes receivable (less allowance for doubtful receivables of \$17,186 in 1996 and \$13,456 in 1995)	285,337	398,515
Regulatory accounts receivable	157,281	260,573
Income taxes receivable	6,962	
Deferred income taxes	63,709	25,953
Gas in storage	20,732	54,782
Materials and supplies	16,225	14,504
Prepaid expenses	9,239	32,593
	-----	-----
Total current assets	559,491	799,531
	-----	-----
Regulatory Assets	438,035	449,521
	-----	-----
Total	\$4,175,537	\$4,462,279
	=====	=====

See Notes to Condensed Consolidated Financial Statements.

SOUTHERN CALIFORNIA GAS COMPANY AND SUBSIDIARY  
 CONDENSED CONSOLIDATED BALANCE SHEET  
 CAPITALIZATION AND LIABILITIES  
 (Thousands of Dollars)

	June 30 1996	December 31 1995
	----- (Unaudited)	-----
<b>Capitalization:</b>		
Common equity:		
Common stock	\$ 834,889	\$ 834,889
Retained earnings	510,668	613,445
	-----	-----
Total common equity	1,345,557	1,448,334
Preferred stock	96,551	196,551
Long-term debt	1,188,390	1,220,136
	-----	-----
Total capitalization	2,630,498	2,865,021
	-----	-----
<b>Current Liabilities:</b>		
Short-term debt	136,342	233,817
Accounts payable	387,309	418,570
Accounts payable-affiliates	87,490	9,734
Accrued taxes and franchise payments	15,967	45,933
Long-term debt due within one year	20,002	95,283
Accrued interest	27,878	43,480
Other accrued liabilities	151,592	50,678
	-----	-----
Total current liabilities	826,580	897,495
	-----	-----
<b>Deferred Credits:</b>		
Customer advances for construction	45,940	47,029
Deferred income taxes	439,584	404,308
Deferred investment tax credits	65,490	66,983
Other deferred credits	167,445	181,443
	-----	-----
Total deferred credits	718,459	699,763
	-----	-----
Total	\$4,175,537	\$4,462,279
	=====	=====

See Notes to Condensed Consolidated Financial Statements.

SOUTHERN CALIFORNIA GAS COMPANY AND SUBSIDIARY  
CONDENSED STATEMENT OF CONSOLIDATED CASH FLOWS  
(Thousands of Dollars)

	Six Months Ended June 30	
	1996	1995
	-----	-----
	(Unaudited)	
Cash Flows From Operating Activities:		
Net income	\$ 89,062	\$ 104,074
Adjustments to reconcile net income to net cash provided by operating activities:		
Depreciation	123,098	118,326
Deferred income taxes	6,635	14,632
Other	(18,421)	6,984
Net change in other working capital components	301,436	284,705
	-----	-----
Net cash provided by operating activities	501,810	528,721
	-----	-----
Cash Flows from Investing Activities:		
Expenditures for utility plant	(84,548)	(97,878)
Decrease in other assets	(225)	21,445
	-----	-----
Net cash used in investing activities	(84,773)	(76,433)
	-----	-----
Cash Flows from Financing Activities:		
Dividends paid	(125,140)	(101,711)
Decrease in long-term debt	(107,027)	(60,729)
Decrease in short-term debt	(97,475)	(194,384)
Redemption of preferred stock	(100,000)	
	-----	-----
Net cash used in financing activities	(429,642)	(356,824)
	-----	-----
Increase in Cash and Cash Equivalents	(12,605)	95,464
Cash and Cash Equivalents, January 1	12,611	57,531
	-----	-----
Cash and Cash Equivalents, June 30	\$ 6	\$ 152,995
	=====	=====
Supplemental Disclosure of Cash Flow Information:		
Cash paid (refunded) during the period:		
Interest (net of amount capitalized)	\$ 56,828	\$ 51,078
	=====	=====
Income Taxes	\$ 124,123	\$ 184,702
	=====	=====

See Notes to Condensed Consolidated Financial Statements.

SOUTHERN CALIFORNIA GAS COMPANY AND SUBSIDIARY  
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (UNAUDITED)

## 1. SUMMARY OF ACCOUNTING POLICIES

The accompanying condensed consolidated financial statements have been prepared in accordance with the interim period reporting requirements of Form 10-Q. Reference is made to the Form 10-K for the year ended December 31, 1995 for additional information.

Results of operations for interim periods are not necessarily indicative of results for the entire year. In order to match revenues and costs for interim reporting purposes, the Southern California Gas Company (Company) defers revenue related to costs which are expected to be incurred later in the year. In the opinion of management, the accompanying statements reflect all adjustments which are necessary for a fair presentation. These adjustments are of a normal recurring nature. Certain changes in account classification have been made in the prior years' consolidated financial statements to conform to the 1996 financial statement presentation.

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

This discussion should be read in conjunction with the Condensed Consolidated Financial Statements contained in this Form 10-Q and Management's Discussion and Analysis of Financial Condition and Results of Operations contained in the Company's 1995 Form 10-K.

Southern California Gas Company (Company) is a subsidiary of Pacific Enterprises (Parent). The Company, a public utility, provides natural gas distribution, transmission and storage in a 23,000-square-mile service area in southern California and part of central California. Company markets are separated into core customers and noncore customers. Core customers consist of approximately 4.7 million customers (4.5 million residential and 200,000 small commercial and industrial customers). The noncore market consists of approximately 1,600 large customers which include 8 utility electric generation, 3 wholesale, and the remainder large commercial and industrial customers. The Company is regulated by the California Public Utilities Commission (CPUC). It is the responsibility of the CPUC to determine that utilities operate in the best interest of the customers with the opportunity to earn a reasonable return on investment.

## RESULTS OF OPERATIONS

Net income for the three and six months ended June 30, 1996 decreased by \$20 million and \$14 million, respectively, compared to the same periods in 1995.

Excluding non-recurring items (described below), results were approximately even with last year.

The Company's earnings decreased primarily due to a one-time non-cash charge of \$26.6 million, after-tax, related to the Comprehensive Settlement of excess gas costs and other regulatory matters.

As part of the Comprehensive Settlement which resolved future excess gas cost issues, the CPUC ruled that rates charged to noncore customers for the five-year period ending August 1, 1999 will be based on actual volumes delivered in 1991. The Company was permitted to retain any revenue enhancements from throughput exceeding these levels subject to a crediting mechanism for revenues in excess of certain limits. The Company estimated the amount of these future revenue enhancements and applied them to reduce the 1993 charge for the Comprehensive Settlement.

As a result of continuing developments in the CPUC's regulatory restructuring of the electric utility industry, the Company now anticipates that throughput to noncore customers will decline from levels projected at the time of the Comprehensive Settlement. Consequently, it believes it will not realize the remaining revenue enhancements that were applied to offset the costs of the Comprehensive Settlement and has charged that amount to revenues resulting in a reduction in earnings of \$26.6 million after-tax. In connection with the 1992 quasi-reorganization, the Parent established a reserve for excess gas costs and consequently, the charge to the Company's income has no effect on Pacific Enterprises' consolidated income. There was no quasi-reorganization for accounting purposes at the Company in 1992, since it is a regulated entity whose assets and liabilities, for the most part, are recorded on the basis of future rate recovery.

This reduction was partially offset by \$13.6 million after-taxes, representing one-time favorable settlements. One settlement is from gas producers for damages incurred to Company and customer equipment as a result of impure gas supplies and the other reflects the resolution of environmental insurance claims which benefited earnings by \$8.0 million.

In the first six months of 1996, noncore throughput fell below levels used by the CPUC in establishing rates as a result of UEG customers being able to purchase abundant, inexpensive hydro-generated electricity produced as a result of abnormally high snow and rainfall this winter. This negatively impacted net income by \$5.1 million, after-tax. Also having a negative effect on earnings was the decrease in the rate of return on common equity from 12.0 percent in 1995 to 11.6 percent in 1996. Both of these were offset by reductions in operating and maintenance expenses.

The Company's operating revenues, excluding the adjustment for the Comprehensive Settlement (described above), for the three and six months ended June 30, 1996 decreased \$35 million and \$20 million, respectively, when compared to the same periods in 1995. Core revenues decreased compared to last year; however, under the current regulatory framework, changes in

revenue resulting from changes in core volumes and cost of gas delivered to the core market do not affect net income. The Company is at risk for reductions in noncore volumes and revenues below those used by the CPUC in establishing rates; therefore, decreases in the UEG throughput due to the availability of inexpensive hydro-generated electricity, resulted in a \$5.1 million negative impact on net income.

Operating and maintenance expenses for the three and six months ended June 30, 1996 decreased \$14 million and \$27 million, respectively, when compared to 1995. The decrease is primarily due to a \$9.5 million pre-tax (\$5.6 million after-tax) settlement from gas producers for damages incurred to Company and customer equipment resulting from impure gas supplies and other reductions in operating and maintenance expenses.

#### RECENT CPUC REGULATORY ACTIVITY

Under the Gas Cost Incentive Mechanism (GCIM), the Company can recover all costs in excess of the benchmark to the extent they fall within a tolerance band which extends to 4 percent above the benchmark. If the Company's cost of gas exceeds the tolerance level, then the excess costs are shared equally between customers and shareholders. All savings from gas purchased below the benchmark are shared equally between customers and shareholders.

The Company's purchased gas costs were \$12.4 million below the specified Gas Cost Incentive Mechanism (GCIM) benchmark for the period April 1995 to March 1996. A filing has been made with the CPUC requesting a \$6.2 million reward for shareholders under the procurement portion of the incentive mechanism.

The Company enters into gas futures contracts in the open market on a limited basis. The Company's intention is to use gas futures contracts to mitigate risk and better manage gas costs. The CPUC has approved the use of gas futures for managing risk associated with the GCIM.

**FACTORS INFLUENCING FUTURE PERFORMANCE.** Under current ratemaking policies, future Company net income and cash flow will be determined primarily by the allowed rate of return on common equity, changes to authorized ratebase, noncore market pricing and the variance in gas volumes delivered to noncore customers versus those used by the CPUC in establishing rates and the ability of management to control expenses and investment in line with the amounts authorized by the CPUC to be collected in rates.

Future regulatory restructuring, increased competitiveness in the industry and the electric industry restructuring will also affect the Company's future performance. The Company has filed a "Performance Based Regulation" (PBR) application with the CPUC to replace the general rate case and certain other regulatory proceedings. This new approach would maintain cost based rates, but would link financial performance with changes in productivity. In May 1996, the Company submitted a supplemental PBR filing to the CPUC proposing that customer rates be reduced by approximately \$61.2 million, or 4% from

current levels. If approved, PBR would be implemented some time after January 1, 1997.

In March 1996, the Company filed its 1996 Biennial Cost Allocation Proceeding with the CPUC. In its filing, the Company is seeking a total rate reduction of \$138 million. The rate reduction reflects amounts previously collected in rates, but not expended for conservation programs, research and development programs and purchased gas costs. A CPUC decision is expected in the fourth quarter.

The Company's earnings for 1996 are being affected by the decrease in the authorized rate of return on common equity, reflecting the overall decrease in cost of capital. For 1996, the Company is authorized to earn a rate of return on ratebase of 9.42 percent and a rate of return on common equity of 11.6 percent compared to 9.67 percent and 12.00 percent, respectively, in 1995. A change in return on equity of 1 percent (100 basis points) impacts net income by approximately \$13 million. The CPUC has also authorized an increase in the equity component of the Company's capital structure to 47.4 percent in 1996 from 47.0 percent in 1995. The 40 basis point increase in the equity component should add between \$1 million to \$2 million to earnings. Rate base is expected to decline slightly from the level in 1995.

On May 8, 1996, the Company filed a request with the CPUC for the 1997 cost of capital. The Company requested an authorized return on common equity of 11.95 percent and 9.74 percent return on rate base. Also requested in the filing was a 60 basis point increase in its authorized common equity ratio to 48.0 percent. The CPUC is expected to issue its decision in the fourth quarter of 1996.

As discussed in the 1995 Form 10-K, existing interstate pipeline capacity into California exceeds current demand by over 1 billion cubic feet per day. Cost of unsubscribed capacity may be charged back to firm customers. However, the Federal Energy Regulatory Commission (FERC) has approved a settlement with Transwestern which calls for firm customers, including the Company, to subsidize unsubscribed pipeline costs for a five-year period with Transwestern assuming full responsibility after that time. A settlement was also reached with El Paso, in which customers, including the Company, will pay for a portion of the unused capacity. The customers may also receive credits from El Paso for unused capacity sold. The settlement is for a ten-year period and is awaiting approval by the FERC.

Most field, clerical and technical employees of the Company are represented by the Utility Workers' Union of America or the International Chemical Workers' Union. An agreement covering these approximately 5,200 employees relating to wages, hours and working conditions expired on March 31, 1996. Negotiations related to a new contract are ongoing. In June, a union decertification petition was filed with the National Labor Relations Board (NLRB) by members of the Company's unions. To date, the NLRB has not ruled on the petition or set a time for the decertification election.

For additional information, see the discussion under the caption "Management Discussion and Analysis - Factors Influencing Future Performance" in the Company's 1995 Form 10-K.

**CAPITAL EXPENDITURES.** For the six months ended June 30, 1996 and 1995, capital expenditures were \$85 and \$98 million, respectively. Capital expenditures for utility plant are expected to be \$225 million in 1996 and will be financed primarily by internally-generated funds.

**LIQUIDITY**

Regulatory accounts receivable decreased \$103 million reflecting the recovery through rates of amounts undercollected in prior years. Cash flows generated through earnings and collections of regulatory accounts receivable, were available for the payment of dividends to the Parent, repayment of commercial paper, repurchase of preferred stock and payment of Swiss Franc bonds.

During the first quarter, the Company redeemed \$50 million of Series A Flexible Auction preferred stock and in the second quarter, redeemed \$50 million of Series C Flexible Auction preferred stock.

On April 30, 1996, investors put back \$67 million of the Company's perpetual Swiss Franc bonds representing 90% of the total \$75 million outstanding. The next available put date for the outstanding balance is the year 2006.

**PART II. OTHER INFORMATION**

**Item 6. EXHIBITS AND REPORTS ON FORM 8-K**

(b) There were no reports of Form 8-K filed during the quarter ended June 30, 1996.

**SIGNATURE**

Pursuant to the requirements of the Securities Exchange Act of 1934, the registrant has duly caused this report to be signed on its behalf by the undersigned thereunto duly authorized.

SOUTHERN CALIFORNIA GAS COMPANY  
-----  
(Registrant)

-----  
Ralph Todaro  
Vice President and Controller  
(Chief Accounting Officer and  
duly authorized signatory)  
Date: July 26, 1996

UT

THE SCHEDULE CONTAINS SUMMARY FINANCIAL INFORMATION EXTRACTED FROM THE CONDENSED STATEMENT OF CONSOLIDATED INCOME, BALANCE SHEET AND CASH FLOWS AND IS QUALIFIED IN ITS ENTIRETY BY REFERENCE TO SUCH FINANCIAL STATEMENTS.

0000092108

SOUTHERN CALIFORNIA GAS COMPANY

1,000

6-MOS	DEC-31-1995	JUN-30-1996
		PER-BOOK
	3,178,011	
	0	
	559,491	
	438,035	
		0
		4,175,537
		834,889
	0	
	510,668	
1,345,557		
	0	
		96,551
	1,188,390	
	136,342	
	0	
	0	
20,002		
	0	
	0	
		0
1,388,695		
4,175,537		
	1,116,940	
	70,823	
	913,084	
	983,907	
	133,033	
		(37)
132,996		
	43,934	
		89,062
	4,675	
84,387		
	0	
	0	
	501,810	
		0
		0