CITY OF LONG BEACH
Gas & Oil
DEPARTMENT

C-9

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February 14, 2006

HONORABLE MAYOR AND CITY COUNCIL
City of Long Beach
California

RECOMMENDATION:

Authorize the City Manager to enter into a natural gas supply agreement with BP Energy Company, Occidental Energy Marketing, Inc., or Coral Energy Resources, L.P. that meets or exceeds the following conditions: 1) full gas volume requirements; 2) term not to exceed three years; 3) annual volume of up to 10 billion cubic feet; 4) a price based upon a Southern California border price index; 5) a November-through-February price ceiling of not greater than $15.00 per Decatherm and an annual price floor of not greater than $8.50 per Decatherm; and 6) a monthly management fee not to exceed $150,000. (Citywide)

DISCUSSION

On March 4, 2003, and March 18, 2003, the City Council authorized the City Manager to enter into a long-term natural gas supply Agreement with Coral Energy Resources, L.P. for the term April 1, 2003 through March 31, 2006 (Coral Agreement). Long Beach Gas & Oil's (LBGO) ability to consistently provide the lowest Southern California residential gas prices over the last three years has been largely the result of the negotiated terms and structure of the Coral Agreement. The terms of the Coral Agreement are as follows:

- A San Juan Basin (a major gas production area in New Mexico) market index plus a $0.36 per Decatherm interstate transportation charge to deliver the gas to the Southern California border
- A November through March price ceiling of $10.00 per Decatherm
- An annual price floor of $3.00 per Decatherm
- A monthly energy management fee of $84,000

Because the Coral Agreement ends on March 31, 2006, LBGO's intention is to obtain a replacement gas supply agreement that results in a gas supply that is comparably priced to those paid by other natural gas utilities in Southern California as well as provides a level of customer price protection against future market price increases. Concerns about potential future supply tightness and pressure from high oil prices are keeping market prices for natural gas much higher than when the Coral Agreement was negotiated three years ago. As a result, it is expected that the replacement agreement may contain terms that reflect the current higher market conditions.

In December 2005, LBGO issued a Request for Qualifications (RFQ) to major natural gas supply providers. After interviewing several suppliers, three finalists were selected based upon their ability to provide secure gas supplies under pricing methodologies that will meet LBGO's objectives. The three finalists are BP Energy Company, Coral Energy Resources, L.P., and Occidental Energy Marketing, Inc.

Each of these companies has an excellent reputation in the industry, has access to major gas supplies, storage capacity, various interstate pipeline transportation rights, and acceptable credit ratings. Based on in-depth discussions with industry experts regarding future market pricing expectations, LBGO desires to enter into a long-term natural gas supply agreement that best meets or exceeds each of the following conditions and is considered preferable to other currently available supply options:

- **TERM:** A term not to exceed 36 months.
- **VOLUME:** Full gas volume requirements (all LBGO gas requirements above the approximately 15 percent procured through local producers).
- **PRICE:** Based upon a Southern California border price market index (with interstate pipeline costs included), which is expected to more closely correspond to the SoCalGas price in the future than the San Juan index currently used as the basis for the Coral Agreement.
- **PRICE CEILING/FLOOR:** A price ceiling of not greater than $15.00 per Decatherm shall apply in the winter months of November – February to ensure the price of gas will go no higher than $15.00 per Decatherm and a price floor of $8.50 per Decatherm shall apply each month to mitigate the cost of the winter ceiling.
- **MONTHLY FIXED PAYMENT:** A monthly fixed payment of not more than $150,000 may be paid by LBGO to the supplier to compensate for services including the cost of the price ceiling, scheduling and balancing of gas supplies transported on the interstate and intrastate pipelines, and the scheduling and balancing of storage services.

This matter was reviewed by Deputy City Attorney Richard Anthony on February 7, 2006 and Budget Management Officer David Wodynski on February 8, 2006.

TIMING CONSIDERATIONS

To take advantage of favorable market conditions, City Council action on this item is requested on February 14, 2006. Authorization by the City Council is requested in advance of finalizing the negotiations with the three finalists. To require a supplier to offer a price that is valid for an extended length of time while City Council approval is sought would result in a much less attractive offer as the supplier would include a substantial premium to protect against potential interim price fluctuations. Once negotiations are concluded, LBGO will return to the City Council to provide the name of the successful supplier and the finalized gas supply terms.

FISCAL IMPACT

Funds associated with the gas supply agreement are budgeted in the Gas Fund (EF 301) in the Long Beach Gas and Oil Department.

SUGGESTED ACTION:

Approve recommendation.

Respectfully submitted,

Christopher J. Garner

CHRISTOPHER J. GARNER
DIRECTOR OF LONG BEACH GAS AND OIL

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APPROVED:

Gerald R. Miller

GERALD R. MILLER
CITY MANAGER