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September 16, 2008

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HONORABLE MAYOR AND CITY COUNCIL
City of Long Beach
California

RECOMMENDATION:

Authorize the City Manager to execute an International Swap and Derivatives Association (ISDA) Master Agreement with Merrill Lynch Commodities, Inc. (MLCI) to authorize various natural gas financial transaction programs, as the City Manager may deem appropriate. (Citywide)

DISCUSSION

Effective November 1, 2007, the Long Beach Gas & Oil Department (LBGO), through the Long Beach Bond Finance Authority, entered into a thirty-year gas prepay contract with Merrill Lynch Commodities, Inc. (MLCI). Under the terms of the contract, MLCI is the primary supplier of natural gas to LBGO. As such, in order to facilitate necessary and beneficial financial transactions related to the purchase of natural gas for LBGO's customers, LBGO requests authorization and approval to enter into an International Swap and Derivatives (ISDA) Master Agreement with MLCI.

An ISDA Master Agreement would allow LBGO to establish programs for the financial swap of the LBGO natural gas pricing index and/or future price protection programs with MLCI. These programs would be secured to provide price reductions and/or price protections for the purchase of natural gas for LBGO's customers.

LBGO expects to utilize the ISDA Master Agreement with MLCI immediately to allow LBGO to swap the current contracted pricing index for a historically lower cost price index. Under the current method, LBGO purchases half of its natural gas volume at the Southern California Gas Company Core Procurement Cost (SoCalGas index) and the other half at NGI Southern California Border Index (Border index). Historically, the Border index has been comparable with the SoCalGas index. However, current gas market conditions have resulted in the Border index averaging \$0.18 less than the SoCalGas index over the past 12 months. An executed ISDA Master Agreement would allow LBGO to alter its pricing method and purchase all of its contracted MLCI volumes at the Border index, which is expected to lead to substantial savings.

HONORABLE MAYOR AND CITY COUNCIL

September 16, 2008

Page 2

This matter was reviewed by Deputy City Attorney Richard Anthony and Budget Management Officer Victoria Bell on August 25, 2008.

TIMING CONSIDERATIONS

City Council action is requested on September 16, 2008, in order to execute an ISDA Master Agreement effective October 1, 2008. This agreement is expected to aid in LBGO's ability to maintain rates that are comparable with those of other like utilities pursuant to Section 1502 of the Long Beach City Charter. The ISDA Master Agreement has no end date. Each party may terminate the agreement at any time by at least thirty days prior written notice to the other party.

FISCAL IMPACT

The ISDA Master Agreement itself does not have any financial impact to the City. Based upon recent price patterns, the anticipated financial swap of the LBGO pricing index will result in approximately \$735,000 of annual savings in natural gas procurement costs. These savings will result in a lower cost of gas for LBGO's customers. Actual savings will vary based on the conditions in the natural gas commodity market.

SUGGESTED ACTION:

Approve recommendation.

Respectfully submitted,



CHRISTOPHER J. GARNER
DIRECTOR OF LONG BEACH GAS & OIL

CJG:LHT:djb

APPROVED:



PATRICK H. WEST
CITY MANAGER