National Association of Regulatory Utility Commissioners

Natural Gas Contracts in New York State

Thomas G. Dvorsky
Director, Office of Gas and Water
New York State Department of Public Service
Thomas_Dvorsky@dps.state.ny.us

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LDC Gas Supply Portfolios

- LDC gas supply portfolios consist of a variety of components
  - Interstate pipeline capacity
    - From producing regions or market area liquid points to the city-gate
  - Storage
    - Market area storage--located closer to the consuming areas
      - e.g., substantial storage fields located in Pennsylvania
    - Production area storage
  - Purchases of gas supply (at the wellhead, at market centers or liquid points and at the city-gate)
  - Arrangements to use the firm supplies of electric and co-generation plants
  - Peaking facilities located within their service territories
    - Liquefied natural gas (LNG)
    - Propane-air (LPG-air) plants

LDC Gas Supply Portfolios

Capacity

- LDCs contract for shipping rights on the pipelines
  - The cost of reserving capacity on these pipelines is a fixed cost and is based on a maximum daily volume of natural gas that may be transported
- LDCs contract for storage capacity and manage filling and withdrawing gas from that capacity
  - Storage plays a significant role in reducing total gas costs as well as providing supply reliability
  - Gas is injected into storage during the summer months, when it has been traditionally lower in price
  - The gas is then withdrawn from the fields to be used during the winter months

LDC Gas Supply Portfolios

Gas Supply

- LDCs maintain a portfolio of gas supply contracts with varying terms of expiration and flexibility
  - Ability to react to changing market conditions
  - For periods ranging from one season to several years
  - Base load contracts
  - Monthly take or release contracts
  - Swing supply contracts
  - Spot or daily purchases
    - Most of the LDCs have minimal reliance on daily purchases
  - Supply contracts generally have pricing mechanisms that allow each company the option to trigger a NYMEX price, use first-of-the-month index prices or negotiate a month or longer fixed commodity price

Peaking Facilities

LNG Facilities

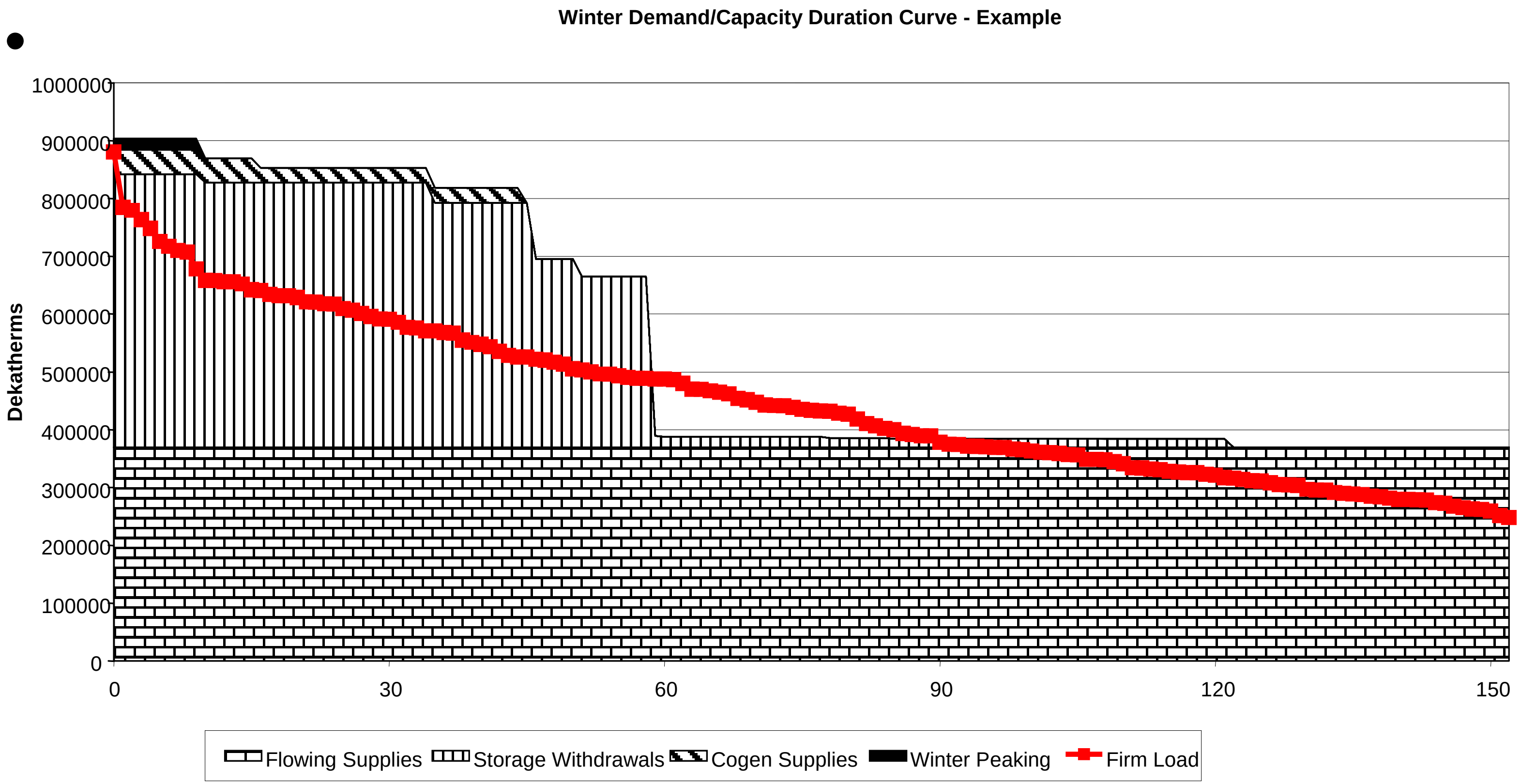
- Natural gas at -260 degrees F is a liquid. Stored at that temperature to keep it in a liquid state, 1/600th of gaseous volume
- LNG facilities provide huge volumes of gas for the very coldest days of the winter
- Inventory of the storage facility can be depleted in just a few days at maximum vaporization rates
- Liquefaction rates are only a small fraction of the vaporization rates; refill takes a whole season to replace

Peaking Facilities

There are three LNG facilities in the State

- Con Edison facility located in Astoria
  - 1050 Mdt capacity
  - 166 Mdt/d vaporization capability
- KeySpan NY facility in Greenpoint
  - 1600 Mdt capacity
  - 291 Mdt/d vaporization capability
- KeySpan LI facility in Holtsville
  - 600 Mdt capacity
  - 103 Mdt/d vaporization capability

Niagara Mohawk

- 

Policy Statement Concerning Gas Purchasing Practices

Background:

- Historically, diversification of LDCs’ supply portfolios was comprised of storage gas and flowing gas from a limited number of supply basins
- Prior to the Policy Statement most LDCs bought natural gas primarily through contracts that reset price monthly on a specified price index (NYMEX or Canadian Weighted Average)
  - Reliance on Index Pricing solely did not recognize or manage price volatility
  - LDCs felt that paying the market price ensured prudence

Policy Statement Concerning Gas Purchasing Practices

Purpose:

- To provide diversity in acquisitions and to defuse price spikes and valleys for gas supplies

Compliance:

- LDCs need to develop an acquisition strategy to include a mix of purchase options with a view toward fostering price stability

Policy Statement Concerning Gas Purchasing Practices

Policy:

- LDCs should consider all available options for purchasing gas and assess the benefits of each approach
- Options may include: short and longer term fixed price purchases, spot acquisitions, use of financial hedges, and contracts providing flexibility in the amount taken over term of the agreement
- Volatility of customer bills is one of the criteria, as well as cost and reliability, that should be considered in purchasing strategies
- Excessive reliance on any one gas pricing mechanism or strategy does not appear to reflect the best management of the gas portfolio
- Any gas utility without a diversified gas pricing strategy will have a heavy burden to demonstrate that its approach is reasonable

Reducing Gas Price Volatility

- Hedging would be setting prices for future deliveries to protect against significant price fluctuations.
- NY LDCs have hedged a significant portion of their gas supply
  - storage inventories provide a natural hedge
  - a portion of flowing gas is hedged either through a physical hedge or a financial hedge

Storage – Natural Physical Hedge

- LDCs provide 25% to 40% of their normal winter supply from storage
- Storage provides a natural hedge
  - Gas is injected into storage from April through October at market prices
  - Gas is withdrawn from storage from November through March at a fixed price (i.e., weighted cost of gas in storage)
- Market area storage is used primarily for city-gate supply, transportation balancing and swing supply services at a fixed gas cost
- Production area storage is also used by a few companies to protect supply from force majeure situations and for price protection of normal flowing supplies

Financial Hedges

- LDCs provide up to 35% of their normal winter supply with financial hedges
- Futures and Options Contracts are purchased to provide the ability to flow gas at a fixed price
- Futures are at fixed prices by delivery month for specified volumes
- Options can be simple calls or puts, collars or cost-less collars, and swaps

Typical Winter Supply Portfolio