This is an informational report and no Council action is required.

BACKGROUND

Last winter’s unprecedented high gas prices and gas market volatility caused staff to develop a structured natural gas purchasing plan. This gas purchasing plan defined the fractions of each month’s gas requirement that are to be purchased over a three-year time horizon. This “laddering” structure was implemented starting in winter 2000, and was described to the Finance Committee via an informational report (CMR:196:01) on April 17, 2001.

Staff presented an information report to the Utilities Advisory Commission (UAC) on December 5, 2001 describing staff’s plan to diverge from the “laddering” structure for fiscal year 2002-03 and purchase 100% of forecasted needs as soon as possible. The UAC was supportive, and staff has implemented the revised plan.

DISCUSSION

Over the past several months, natural gas prices have dropped sharply from levels seen last winter. Prices are projected to be about one fourth of last year’s peak price. This
decline is due to weather, an increase in gas storage, and a slumping economy. Staff recognized an opportunity to purchase more gas for fiscal year 2002-03 at this time than what was envisioned in the “laddering” structure, when prices can rise much more than they can fall. Additionally, this will lead to greater cost and commodity budget certainty and will enable staff to make rate-setting and budget-making decisions with less risk.

To that end, staff has deviated from the “laddering” approach and purchased, at fixed prices, gas for CPAU’s customers who are not eligible to choose an alternative gas commodity supplier. Purchasing the majority of the City’s natural gas requirements at fixed prices will reduce the market price risk, but not totally eliminate gas cost uncertainty. Additional gas, above the forecasted volumes, will be purchased at the market price. Also, gas for those large customers who may choose an alternative commodity supplier will be purchased either at the monthly market price (for those customers who elect a market rate) or at a fixed price at the time of selecting a fixed-term rate. These large customers account for approximately 23% of the total load and account for the uncertainty remaining in the total gas cost.

**RESOURCE IMPACT**

The budget for fiscal year 2002-03 is currently set at $28 million, approximately 13% less than the fiscal year 2001-02 budgeted cost of $32 million. Under the original “laddering” goal for fiscal year 2002-03, the range of possible total gas costs was between $11 million and $31 million. The large range is attributed to having a large portion of the gas load exposed to fluctuating wholesale market prices. As a result of purchasing approximately 100% of expected load under the revised plan at current low market prices, the total expected cost for fiscal year 2002-03 is $15 million and the range of possible costs has narrowed from between $14.4 million and $17 million. In the coming months staff will present to Council a retail rate decrease proposal that passes on these budget savings to customers.

**POLICY IMPLICATIONS**

The revised gas purchasing plan for fiscal year 2002-03 diverges from the original “laddering” approach previously reviewed by Council. The revised plan was implemented to achieve additional cost savings and rate certainty. The revised plan is
consistent with the Council approved Utilities Strategic Plan to provide a supply cost advantage compared to the market price and to maximize the General Fund transfers and maintain financial strength.

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