

PURCHASE NATURAL GAS FROM A THIRD PARTY SUPPLIER

By purchasing natural gas from a third party supplier, significant cost savings are possible. The local utility is not always making decisions in your favor and does not necessarily have the incentive to reduce costs. It is expected that at least \$1.25 to \$2.25 per MMBtu savings is achievable. This savings is based on natural gas prices that other manufacturers in the certain areas have achieved by contracting with third party natural gas marketers. There are many natural gas marketers that are capable of supplying natural gas at competitive prices. Properly contracted, the marketer will work to supply you with the lowest cost and minimize your risk.

Getting natural gas from the wellhead to your burner tip is a long and complicated process; however, it is vital to understand these fundamentals to be able to talk the language of natural gas marketers. Each step along the way or pipeline bears a cost. A breakdown in cost for natural gas is shown in Figure 1-1. This figure is shown just for illustrative purposes and the prices are not meant to reflect your actual costs. As shown, there are a lot of costs associated with natural gas purchasing. However, the cost can be broken down into 3 major categories: 1) spot price or commodity price, 2) transportation basis, and 3) LDC cost. The spot price or commodity cost is by far the largest cost component (typically 50% to 75% of the total). This cost component deserves the most attention by the end-user. The transportation basis is the cost of moving the gas on the interstate pipelines to get the gas molecules from the wellhead to the “city gate”. This cost is regulated and usually fixed. It is public knowledge and can be obtained from an electronic bulletin board published by the interstate transmission pipeline. The LDC or utility cost is paid for moving the molecule from the “city gate” to your burner tip.

The contracting process can be complex. If natural gas purchasing is alien to your company, then it is suggested that a consultant be hired to help you with the process. Most marketers have standard contracts. However, these contracts do not always reflect the needs of the end-user. All contracts should be buyer initiated! The marketer may simply wish to take the easy route and purchase gas for you and supply it to the city gate. However, it is important to know how to compose contract language and whether you would like the marketer to manage the gas for you (called nominating), to manage interactions with the LDC, to hedge your commodity cost, etc. A consultant would be appropriate to hire if any of these tasks are beyond your current ability.

FIGURE 1-1
Typical Gas Costs for Transporting Gas on Interstate Pipelines

<u>1. Wellhead cost of gas per Dth/MMBtu</u>			
(Pricing Point #1)			<u>\$ 2.01</u>
2. Third party charge			
Per Dth/MMBtu	<u>\$ 0.04</u>	}	
3. Interstate transportation cost, Firm			
Per Dth/MMBtu	<u>\$ 0.30</u>		
4. Natural gas shrinkage			
Per Dth/MMBtu	<u>\$ 0.05</u>		
5. Miscellaneous charges			
Per Dth/MMBtu	<u>\$ 0.025</u>		
<u>Interstate / City Gate Price</u>			
(Total of Items 1 – 5) cost per Dth/MMBtu			
(Pricing Point #2)			<u>\$ 2.425</u>
6. Intrastate transportation			
Cost per Dth/MMBtu	<u>\$ 0.80</u>	}	
7. Natural Gas Shrinkage			
	<u>\$ 0.04</u>		
8. Miscellaneous charges			
Per Dth/MMBtu	<u>\$ 0.025</u>		
<u>End-user Customer Burner Tip Cost</u>			
(Total of Items 1 – 9) per Dth/MMBtu			
(Pricing point #3)			<u>\$ 3.29</u>

**Transportation
Basis**

**LDC
Cost**

EXAMPLE

The average burner tip cost of natural gas for the two largest natural gas accounts at the finishing plant was \$4.70 per MMBtu and \$5.72 per MMBtu was the actual average price for the 12 months studied. The first cost is for an interruptible gas account. The second cost reflects firm gas use. The total gas consumption for the two accounts was 47,468 MMBtu at a cost of \$238,193.

$$CS = GC \times (AC - BT)$$

CS = Cost Savings

GC = Gas Consumption

AC = Actual Cost

BT = Burner Tip Cost

For the above example,

$$\begin{aligned} &= 47,468 \text{ MMBtu} \times (\$5.72/\text{MMBtu} - \$4.70/\text{MMBtu}) \\ &= \$48,417/\text{year} \end{aligned}$$

IMPLEMENTATION COST

It is advisable that some form of back-up system be enacted before this measure is implemented.