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## CONSOL's fuel-flexible contract aims to reduce losers in bets on coal versus gas

By [Taylor Kuykendall](#)

Coal and natural gas producer [CONSOL Energy Inc.](#) is hoping a new fuel-flexible contract it has struck with a customer will provide a workaround to the traditional win-lose nature that stems out of contracts in which utilities and fuel suppliers try to bet on the future price of coal or gas.

CONSOL's experiment with a new sort of contract — one that allows the unnamed utility to take either coal or gas on a monthly basis — was [announced](#) in CONSOL's first-quarter earnings report. In an interview with SNL Energy, Jim McCaffrey, senior vice president of sales for CONSOL, said that as far as he knows, CONSOL is the only provider in the industry that is able to offer such flexibility to its customers.

"Contracts in the past have often been win-lose: Someone guesses right, someone guesses wrong and ends up with a lower price than market or a higher price than market, and one party is happy and the other party is not," McCaffrey said. "We're seeking out innovative ways to make sure that we have — I know it sounds trite, but it's true — more win-win relationships where our customers and CONSOL win together or lose together, but that we're tied more closely at the hip."

McCaffrey said that CONSOL believes the "way of the future" is to work closely with end-user customers on creating contracts and deals that benefit both companies.

"On a monthly basis we have a methodology to choose a forward gas price for the ensuing month," McCaffrey said, noting he was simplifying the mechanics of the contract somewhat. "It doesn't come specifically off an index, but it has an index involved with it. That gas price is submitted to the customer and then the customer has a proprietary formula that they use to calculate what their exact demand is and whether they'd prefer that in coal or gas."

At that point, a price is set on the coal the gas. CONSOL can choose to accept the coal price and ship the coal or it can accept the natural gas price and ship that along instead.

One of the challenges of such a contract, he said, is that coal is a much less liquid commodity than gas and not knowing exact volumes can pose a challenge in allocating resources and determining production levels from the company's [fleet](#) of coal mines. The deal, McCaffrey said, is "relatively small," but "not insignificant."

CONSOL is experimenting with the innovative contract in response to a "general buzz" among the industry since CONSOL made a deal in 2010 [to acquire Dominion Resources Inc.](#)'s Appalachian natural gas business segment.

"To be perfectly honest with you, for several years we were just trying to sort out how to do that and if it made sense. ... I would expect that I will be asked by several people about the deal," said McCaffrey, who was preparing to travel to a fuel buyers conference.

He said given the current state of the market, one would probably expect most of the energy shipped under the deal to be from gas. He declined to say which utility struck the deal, but mentioned the utility had expressed interest in the flexibility of adjusting its fuel buys based on the market.

"They had a desire and we had the flexibility," McCaffrey said. "We're kind of the perfect match and we've done business before."

During the company's earnings call, one executive mentioned that CONSOL was also in talks with another customer over a similar contract. CONSOL President and CEO Nick Deluliis said on the company's recent earnings call that the company "won't be bound by the past" and will embrace the "shifting nature of the energy business."

In an April 29 note, Sterne Agee analyst Michael Dudas noted that the agreement reflects the "strength of diversified low-cost asset base."