





# Metro

MAY 13, 2010

TO: BOARD OF DIRECTORS

THROUGH: ARTHUR T. LEAHY   
CHIEF EXECUTIVE OFFICER

FROM: TERRY MATSUMOTO   
CHIEF FINANCIAL SERVICES OFFICER AND TREASURER

SUBJECT: NATURAL GAS HEDGING PROGRAM

## ISSUE

The Natural Gas Hedging Program (the "Hedging Program") requires that reports be provided to the Board quarterly in compliance with the Hedging Program guidelines and to report performance of the program.

## DISCUSSION

The purpose of this report is to present the status of compliance and performance for the hedged portion of our compressed natural gas (CNG) budget. Operations related variances are presented in order to provide an overall perspective for CNG costs.

The objective of the Hedging Program is to provide "budget certainty" for fuel and to help establish the CNG budget in the upcoming year by locking in most of the cost in advance. Budget certainty is accomplished by utilizing a hedging instrument known as a commodity swap to hedge most of the planned volume for each fiscal year.

As of March 31, 2010, we had executed three of five planned hedge transactions for FY11. A summary of the currently outstanding hedge transactions is provided below. The positive/(negative) market values indicate the amount we would receive/(pay) on an early termination at the specified date. The rates listed in the table below reflect the hedge contract fixed rates and exclude the delivery cost and state mandated charges, which are currently \$0.104 per therm.

Quarterly Summary of Outstanding Hedge Transactions  
Valuation as of March 31, 2010

Period Hedged	Provider	Credit Ratings (S&P, Moody's, Fitch)	Contract Fixed Rate per Therm	Remaining Therms	Current Market Value*
FY10	B of A, NA	A+/Aa3/A+	\$0.8500	218,400	-\$988,448
FY10	BP Corp North America	AA/Aa2/----	\$1.0120	218,400	-\$1,332,854
FY10	BP Corp North America	AA/Aa2/----	\$1.0650	218,400	-\$1,447,820

FY10	BP Corp North America	AA/Aa2/----	\$0.9420	218,400	-\$1,181,012
FY10	RBC Capital Markets	AA-/Aaa/AA	\$0.8265	218,400	-\$930,472
FY10	BP Corp North America	AA/Aa2/----	\$0.6390	303,300	-\$727,356
FY11	Barclays Capital	AA-/Aa3/AA-	\$0.6480	1,314,000	-\$2,099,394
FY11	B of A, NA	AA-/Aa3/AA-	\$0.6530	1,314,000	-\$2,163,021
FY11	Barclays Capital	A+/Aa3/A+	\$0.6075	876,000	-\$1,056,0123
Total			\$0.7064	4,899,300	-\$11,926,390

\*Monthly LIBOR rate used.

## Compliance

As the result of uncertainty about the amount of reduction to bus service in FY11 and FY12, hedging was curtailed at 70% of planned therms for FY11 and has not been initiated for FY12. Otherwise, as of the date of this report the Hedging Program is in compliance with all the specified limitations and requirements. The individual compliance items are listed on Attachment A.

## Performance

For the quarter, CNG costs were \$1,018,900 under budget as a result of a \$619,800 favorable variance for hedge performance, plus a favorable \$399,100 variance for unhedged therms. The favorable variance for unhedged therms resulted from the significant under run in therms usage, allowing us to avoid the purchase of 408,300 therms that were budgeted. For the quarter, due to the under run in therms usage, the hedge ratio was 100%. See Attachment B. The quarterly performance reports for the 1<sup>st</sup> and 2<sup>nd</sup> quarters of FY10 were inadvertently not previously sent to the Board. The Cost Variance pages from those reports are included in this report as Attachments C and D.

Hedge performance for the quarter was favorable by \$619,800 because the variable rates received from the hedge were more than the monthly rates paid to the Gas Company. Hedge performance is our fixed rate payments to the hedge provider, plus actual payments for gas purchases, minus variable rate payments received from the hedge provider at the monthly index rates.

For information purposes only, if we had not hedged the CNG, the variance would have been a favorable \$5,488,000, as opposed to a favorable \$1,018,900. The difference is the result of the lower market rate of \$0.63 during the quarter compared to the hedged rate of \$0.97. Therefore hedging produced a cost about \$4,469,000 more than if we had not hedged.

For the 3<sup>rd</sup> quarter of FY10 the hedging program generally performed as intended and stabilized the actual rate per therm at \$0.97, slightly under the budgeted rate of \$0.98. During the quarter the rates from the Gas Company ranged from \$0.52 to \$0.69 per therm.

## **NEXT STEPS**

- Determine whether to take additional bids for hedges for the remainder of FY11.

## **ATTACHMENTS**

- A. Program Compliance
- B. Quarterly Summary of CNG Costs and Variances

Prepared by: Michael J. Smith, Assistant Treasurer  
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## Attachment A

### Program Compliance

**Maximum Trade Maturity** – was 15 months vs. policy max of 30

**Hedge Ratio** – for FY10 is 97.1% vs. policy range of 90% to 100%

**Maximum Trade Amount** – All trade amounts have been in compliance with the Hedging Program guidelines.

**Frequency of Trades** – No bids were taken during the quarter. We are holding off on entering into any additional trades until Operations develops revised CNG terms usage plans for FY11 and FY12. When we receive the revised terms usage plans we will then determine how best to resume our hedge bidding cycle. The policy provides a range of two to six bids per year. Currently, three bids have been taken for the FY11 and no bids for FY12.

**Timing of Trades** – The policy sets a goal to have the timing of trades equally spaced and occur approximately every other month. The potential for significant changes in the level of bus service, being considered to address the budget shortfall, has caused us to delay the timing for any remaining hedges.

**Counterparty Credit Ratings** – There have been no changes in the credit ratings of the counterparties since the last quarterly report.

Summary of Credit Ratings  
(S&P/ Moody's / Fitch)

Provider	For Current Report FY10-Q3
Bank of America, N.A.	A+/Aa3/A+
Barclays Bank PLC	AA-/Aa3/AA-
BP Corp. North America	AA/Aa2/---
RBC Capital Markets	AA-/Aaa/AA

**Collateral Requirements** – Requirements to post collateral are based on credit ratings of the counterparties. The threshold is \$25 million for counterparties rated “A-/Aa3” or better. The current market values of the trades are under the \$25 million threshold, so no collateral is required.

**Re-Confirm Assumptions** – Assumptions have been reconfirmed for factors that would affect the Gas Company’s cost of gas and reduce the correlation between the Gas Company’s cost and the pricing index the hedges are tied to. There have not been any changes that would cause us to change our assumptions. However, there has been a trend for the past twenty-four months where the Gas Company’s rates have moved slightly higher relative to the hedge index, resulting in a small cost variance. To date, the Gas Company has not been able to provide a good explanation for this trend.

**Re-Confirmation of Therms** - The officially planned amount of therms for FY10 and FY11 currently remain unchanged from the values previously provided by the Operations staff based on the projected service levels. However, given the possibility for service adjustments, the amount of therms will need to be reconfirmed prior to entering into any further hedges for FY11.

All information is as of March 31, 2010, unless otherwise specified.

**Attachment B**

**Quarterly Summary of CNG Costs and Variances  
FY 2010 Q3**

	Budget	Actual	Difference Fav/(Unfav)
<b>Hedged</b>			
Therms	13,680,000	13,159,952	520,048
Fixed Rate Payments	\$ 13,372,201	\$ 11,982,600	
Cost of Gas		\$ 8,283,069	
Variable Rate Payments Received		\$ (7,513,232)	
Basis Variance		\$ 769,837	
Hedge Performance	\$ 13,372,201	\$ 12,752,437	\$ 619,764
Cost/Therm	\$ 0.978	\$ 0.969	\$ 0.008
<b>Unhedged</b>			
Therms	408,322	-	408,322
Cost of Gas	\$ 399,135	\$ -	\$ 399,135
Cost/Therm	\$ 0.978	\$ -	\$ 0.978
<b>Total</b>			
Therms	14,088,322	13,159,952	928,370
Cost of Gas	\$ 13,771,335	\$ 12,752,437	1,018,898
Cost/Therm	\$ 0.978	\$ 0.969	\$ 0.008
Hedge Ratio	97.1%	100.0%	
<b>If No Hedging</b>			
Therms	14,088,322	13,159,952	928,370
Cost of Gas	\$ 13,771,335	\$ 8,283,069	\$ 5,488,266
Cost/Therm	\$ 0.978	\$ 0.629	\$ 0.348
Hedged vs. Un- hedged Difference -		\$ (4,469,368)	

Note: All per therm amounts include \$0.104 for mandated fees and delivery costs

**Attachment C**

**Quarterly Summary of CNG Costs and Variances  
FY 2010 Q2**

	Budget	Actual	Difference Fav/(Unfav)
<b>Hedged</b>			
Therms	13,984,000	13,931,176	52,824
Fixed Rate Payments	\$ 13,669,361	\$ 11,908,082	
Cost of Gas		\$ 8,179,053	
Variable Rate Payments Received		\$ (5,969,173)	
Basis Variance		\$ 2,209,880	
Hedge Performance	\$ 13,669,361	\$ 14,117,962	\$ (448,601)
Cost/Therm	\$ 0.978	\$ 1.013	\$ (0.036)
<b>Unhedged</b>			
Therms	657,492	-	657,492
Cost of Gas	\$ 642,698	\$ -	\$ 642,698
Cost/Therm	\$ 0.978	\$ -	\$ 0.978
<b>Total</b>			
Therms	14,641,492	13,931,176	710,316
Cost of Gas	\$ 14,312,059	\$ 14,117,962	194,097
Cost/Therm	\$ 0.978	\$ 1.013	\$ (0.036)
Hedge Ratio	95.5%	100.0%	
<b>If No Hedging</b>			
Therms	14,641,492	13,931,176	710,316
Cost of Gas	\$ 14,312,059	\$ 8,179,053	\$ 6,133,006
Cost/Therm	\$ 0.978	\$ 0.587	\$ 0.390
<b>Hedged vs. Un-hedged</b>			
Difference - Fav/(Unfav)		\$ (5,938,909)	

Note: All per therm amounts include \$0.104 for mandated fees and delivery costs

**Attachment D**

**Quarterly Summary of CNG Costs and Variances  
FY 2010 Q1**

	Budget	Actual	Difference Fav/(Unfav)
<b>Hedged</b>			
Therms	14,473,000	14,166,704	306,296
Fixed Rate Payments	\$ 14,147,358	\$ 12,561,108	
Cost of Gas		\$ 6,819,002	
Variable Rate Payments Received		\$ (4,456,907)	
Basis Variance		\$ 2,362,095	
Hedge Performance	\$ 14,147,358	\$ 14,923,203	\$ (775,845)
Cost/Therm	\$ 0.978	\$ 1.053	\$ (0.076)
<b>Unhedged</b>			
Therms	340,879	-	340,879
Cost of Gas	\$ 333,209	\$ -	\$ 333,209
Cost/Therm	\$ 0.978	\$ -	\$ 0.978
<b>Total</b>			
Therms	14,813,879	14,166,704	647,175
Cost of Gas	\$ 14,480,567	\$ 14,923,203	(442,635)
Cost/Therm	\$ 0.978	\$ 1.053	\$ (0.076)
Hedge Ratio	97.7%	100.0%	
<b>If No Hedging</b>			
Therms	14,813,879	14,166,704	647,175
Cost of Gas	\$ 14,480,567	\$ 6,819,002	\$ 7,661,565
Cost/Therm	\$ 0.978	\$ 0.481	\$ 0.496
Hedged vs. Un- hedged Difference - Fav/(Unfav)		\$ (8,104,201)	

Note: All per therm amounts include \$0.104 for mandated fees and delivery costs