

FUEL PRICE RISK MANAGEMENT POLICY REPORT

"FUEL HEDGE"

Mar-17

FUEL PRICE RISK MANAGEMENT POLICY REPORT

Mar-17

(Office of Management and Budget 03/31/2017)

The Fuel Price Risk Management Policy approved by the Board on February 16, 2006 requires monthly reports to the Finance/Audit Committee. Per the Finance Chair in 2009, the report is to be presented quarterly to the F/A committee. The Board has approved resolutions authorizing implementation of the Fuel Hedge Policy for FY2008 (October 2006). In July 2008 the Board amended the Fuel Risk Management Policy by eliminating the July 15 deadline for hedging the next fiscal years fuel requirement.

Per the METRO Fuel Price Risk Management Policy, "METRO will minimize operating budget variance attributable to fuel price variability through physical forward contracts and/or financial contracts. METRO will develop and implement a plan which will provide fuel and energy commodity price certainty for up to 24 months of expected consumption such that the operating budget expense is assured with some potential to realize savings if prices decline."

All hedges will be constructed to qualify for hedge accounting treatment under Financial Accounting Standards Board (FASB) guidelines. This means that any financial hedge instrument must settle against, or directly link to, the index used as the pricing reference in the applicable procurement contract. For example, if METRO has a contract for delivery of fuel based on Platt's Gulf Coast Low-Sulfur Diesel Index, the financial hedge must reconcile to Platt's Gulf Coast Low-Sulfur Diesel Index.

A. Diesel Fuel Hedges

Also per METRO's Fuel Price Risk Management Policy, the Authority's Diesel Fuel Hedge Strategy Team, referred to here as "Team", makes hedging decisions on METRO's behalf. The Team is lead from the Procurement department's perspective, and is comprised of Operations, Finance, Procurement, and the Executive Office staff. The Team's objective is to strategically enter into agreements that cover 80% - 90% of projected fuel requirements. Actions and correspondence are typically conducted and documented via email, and the Team convenes as needed. Upon agreement by vote, the Office of Management and Budget, and Procurement department work together to initiate and execute Financial Hedge Swap Agreements.

For FY2017 nine hedges totaling 9.996M gallons were executed at an average price of \$1.8780. For FY2018, eight hedges totaling 10.500M gallons at an average price of \$1.4102 were executed. As of March 31, 2017, one hedge totaling 0.840M gallons at an average price of \$1.5934 has been executed for FY2019. (Hedge prices are market price only, not including transportation, additive and taxes). See Attachment A for hedge details. METRO currently has chosen Merrill Lynch Commodities Inc., and Goldman, Sachs & Co. to bid financial hedges. A comparison of the FY2017 hedged gallons, actual usage and hedge collections is outlined in Attachment B. Hedge payments fiscal year to date total \$2.176M.

B. 5 Year Contract for Electricity

In May 2015 the Board authorized the President and CEO to execute and deliver a contract for electricity provider services for an amount not-to-exceed \$26,491,835, with a 25% energy component and an option to participate in demand response services. The contract was awarded in June 2015 to GDF SUEZ Energy Resources NA Inc. (Suez) to supply electricity for 5 years beginning June 2015 to June 2020. The contract rate of \$.03841 per kilowatt hour was fixed for the term of contract while the Transmission and Distribution (TDSP) charges may vary depending on the Texas Utilities Commission policies.

This contract hedges METRO's electricity requirements for 5 years, providing budget certainty on price in accord with the Board's Fuel Price Risk Management Policy adopted February 2006.

ATTACHMENT A

METRO
FY2017, FY2018 and FY2019 Fuel Hedge (Diesel) - Status 03/31/2017
(Office of Management and Budget 03/31/2017)

Financial Hedge (Oct-Sep Delivery)

| | <u>Delivery</u> <u>Year</u> | <u>Gallons</u> | <u>Fuel Type</u> | <u>Vendor</u> | <u>Date of</u> <u>Purchase</u> | <u>Avg. Price</u> <u>per gallon</u> | <u>Cost</u> |
|---|--------------------------------|----------------|------------------|----------------------|-----------------------------------|--|---------------|
| 1 | FY2017 | 420,000 | USLD | Merrill Lynch | 10/7/14 | \$2.6005 | \$ 1,092,202 |
| 2 | FY2017 | 210,000 | USLD | Merrill Lynch | 10/16/14 | \$2.4871 | \$ 522,291 |
| 3 | FY2017 | 840,000 | USLD | Goldman, Sachs & Co. | 12/19/14 | \$2.0275 | \$ 1,703,100 |
| 4 | FY2017 | 420,000 | USLD | Goldman, Sachs & Co. | 1/22/15 | \$1.8225 | \$ 765,450 |
| 5 | FY2017 | 2,100,000 | USLD | Merrill Lynch | 6/8/15 | \$1.9820 | \$ 4,162,200 |
| 6 | FY2017 | 1,932,000 | USLD | Merrill Lynch | 7/2/15 | \$1.9640 | \$ 3,794,494 |
| 7 | FY2017 | 2,016,000 | USLD | Merrill Lynch | 7/17/15 | \$1.8225 | \$ 3,674,215 |
| 8 | FY2017 | 1,218,000 | USLD | Goldman, Sachs & Co. | 8/11/15 | \$1.7320 | \$ 2,109,530 |
| 9 | FY2017 | 840,000 | USLD | Merrill Lynch | 1/20/16 | \$1.1292 | \$ 948,528 |
| | | 9,996,000 | | | | \$1.8780 | \$ 18,772,009 |
| 1 | FY2018 | 2,520,000 | USLD | Merrill Lynch | 1/20/16 | \$1.1290 | \$ 2,844,954 |
| 2 | FY2018 | 3,486,000 | USLD | Merrill Lynch | 5/9/16 | \$1.4585 | \$ 5,084,331 |
| 3 | FY2018 | 1,470,000 | USLD | Goldman, Sachs & Co. | 7/22/16 | \$1.5375 | \$ 2,260,125 |
| 4 | FY2018 | 1,554,000 | USLD | Merrill Lynch | 8/1/16 | \$1.4805 | \$ 2,300,697 |
| 5 | FY2018 | 252,000 | USLD | Goldman, Sachs & Co. | 8/31/16 | \$1.6105 | \$ 405,846 |
| 6 | FY2018 | 672,000 | USLD | Goldman, Sachs & Co. | 9/1/16 | \$1.5700 | \$ 1,055,040 |
| 7 | FY2018 | 378,000 | USLD | Merrill Lynch | 11/4/16 | \$ 1.5794 | \$ 597,013 |
| 8 | FY2018 | 168,000 | USLD | Goldman, Sachs & Co. | 3/10/17 | \$ 1.5440 | \$ 259,392 |
| | | 10,500,000 | | | | \$1.4102 | \$ 14,807,398 |
| 1 | FY2019 | 840,000 | USLD | Merrill Lynch | 11/4/16 | \$ 1.5934 | \$ 1,338,456 |

ATTACHMENT B

METRO
FY2017 DIESEL FUEL

(Office of Management and Budget 03/31/2017)

| Month | Fuel Source | Gallons in Financial Hedge | Gallons Purchased | Gallons Used | Gallons Used Variance ⁽¹⁾ | Swap Receipts From/ (Payments To) Trader/s |
|--------------|--------------------|---|------------------------------|-------------------------|---|---|
| Oct-16 | Financial Hedge | 840,000 | 979,536 | 1,112,201 | 272,201 | \$ (708,788) |
| Nov-16 | Financial Hedge | 798,000 | 995,464 | 947,738 | 149,738 | \$ (411,743) |
| Dec-16 | Financial Hedge | 756,000 | 936,797 | 915,854 | 159,854 | \$ (259,451) |
| Jan-17 | Financial Hedge | 798,000 | 878,046 | 921,620 | 123,620 | \$ (198,408) |
| Feb-17 | Financial Hedge | 714,000 | 862,369 | 871,291 | 157,291 | \$ (234,683) |
| Mar-17 | Financial Hedge | 840,000 | 1,002,793 | 1,016,731 | 176,731 | \$ (363,590) |
| Apr-17 | Financial Hedge | | | | | |
| May-17 | Financial Hedge | | | | | |
| Jun-17 | Financial Hedge | | | | | |
| Jul-17 | Financial Hedge | | | | | |
| Aug-17 | Financial Hedge | | | | | |
| Sep-17 | Financial Hedge | | | | | |
| Total | | 4,746,000 | 5,655,005 | 5,785,434 | 1,039,434 | \$ (2,176,663) |

NOTE

1. The gallons above the financial hedge volumes, as shown in the variance, were bought at the prevailing market prices.