Eight Steps to Improved Natural Gas Hedges

Procurement and budgeting of natural gas should be the responsibility of the end-user company authorized personnel; however, assistance should be solicited from the company's energy consultant and suppliers. To avoid higher costs and contract violations, experience suggests these eight hedge guidelines:

1) **Companies should be responsible for** commitments for exchange, purchases for resale, purchases to settle imbalances, and commitments for energy purchase to fulfill the purchase obligations of its gas service contracts. Companies should submit all agreements with interstate pipeline, gas suppliers, and regulated utility to their law department for approval.
2) **Companies should practice the highest standards** of ethics and diligence in selecting energy suppliers, placing orders (nominations), balancing usage with orders, and paying invoices.
3) **Hedges should include only natural gas volumes** that are expected and budgeted to be purchased, and should only be placed by authorized personnel when rational, defensible and economically-based market conditions exist and are documented. Mark-to-market analyses should be performed as needed under FASB 133.
4) **Company should form a hedge committee** consisting of a minimum of three officers and/or managers. The Hedge Committee should meet monthly to review the status of the natural gas purchasing strategies. A minimum of two members of the Hedge Committee should be on the phone to confirm transactions which involve the purchase of gas unless prior written approval (including emails approving price targets) is provided. If a transaction exceeds six months, the company should require the written approval of one or more designated hedge committee members.
5) **Any recommendations for a fixed price** should be preceded by discussions with the contracted energy supplier and energy consultant(s.) The company should provide credit support from its business operations without a parental guarantee in an amount not to exceed the likely cost of energy purchases in the form negotiated with the gas supplier.
6) **The energy consultant should provide** support to the company reviewing contracts, market options, and purchase opportunities; recommending action; and documenting decisions for conformance with FASB 133.
7) **The gas supplier should provide** "indicative" prices for the company's consideration and accept the hedge request for a fixed price of natural gas at a specific delivery location during New York Mercantile Exchange hours. Depending on market liquidity and credit considerations, the gas supplier should "lock in" a fixed price for the desired period, provide a confirmation and use the fixed price in its billing for the appropriate period. The gas supplier should be responsible for all daily margin calls and other NYMEX transactions. The gas supplier should supply the contracted volumes of natural gas, provide balancing and market information, and participate in strategy discussions to ensure its contract is performed in an economical manner.
8) **The regulated utility should transport** natural gas purchased into its pipeline system and company service locations, meter it, deliver it, and bill for the volume and quality contracted by the company as regulated by the State regulatory authority.