

**INTERMOUNTAIN GAS COMPANY**

555 SOUTH COLE ROAD • P.O. BOX 7608 • BOISE, IDAHO 83707 • (208) 377-6000 • FAX: 377-6097

RECEIVED  
FILED



2005 SEP -1 PM 4: 20

IDAHO PUBLIC  
UTILITIES COMMISSION

September 2, 2005

Ms. Jean Jewell  
Commission Secretary  
Idaho Public Utilities Commission  
472 W. Washington St.  
P.O. Box 83720  
Boise, Idaho 83720-0074

RE: Intermountain Gas Company  
Case No. INT-G-04-2  
IPUC Order No. 29540

Dear Ms. Jewell:

Enclosed for filing with this Commission are an original and seven copies of Intermountain Gas Company's Gas Supply Risk Management Program – Objectives, Policy, Guidelines & Procedures.

The above referenced Order No. directed the Company and Commission Staff to work together in developing a risk management strategy that would accomplish certain goals and objectives as outlined in the Order. The attached Program represents the culmination of those efforts by the Company and Staff.

Intermountain is committed to work with the Staff on an ongoing basis to enhance and refine the enclosed document as necessary to adapt to the changing marketplace.

If you have any questions or require additional information regarding the attached, please contact me at 377-6168.

Very truly yours,



Michael P. McGrath  
Director  
Gas Supply and Regulatory Affairs

MPM/bf

Enclosures

Cc W. C. Glynn  
P. R. Powell  
M. E. Rich  
M. W. Richards

RECEIVED   
FILED

2005 SEP -1 PM 4: 20

IDAHO PUBLIC  
UTILITIES COMMISSION

# **INTERMOUNTAIN GAS COMPANY**

## **GAS SUPPLY RISK MANAGEMENT PROGRAM**

### **OBJECTIVES, POLICY, GUIDELINES & PROCEDURES**

**INTERMOUNTAIN GAS COMPANY  
GAS SUPPLY RISK MANAGEMENT PROGRAM  
OBJECTIVES, POLICY, GUIDELINES AND PROCEDURES**

**TABLE OF CONTENTS**

	<u>Page</u>
<b>I. PROGRAM OBJECTIVES .....</b>	<b>1</b>
<b>II. ORGANIZATIONAL STRUCTURE.....</b>	<b>1</b>
<b>A. BOARD OF DIRECTORS .....</b>	<b>1</b>
<b>B. PRESIDENT .....</b>	<b>2</b>
<b>C. GAS SUPPLY RISK MANAGEMENT COMMITTEE .....</b>	<b>2</b>
<b>III. ADEQUATE AND RELIABLE NATURAL GAS SUPPLIES, STORATE AND TRANSPORTATION.....</b>	<b>2</b>
<b>IV. MITIGATE THE ADVERSE IMPACT OF COMMODITY PRICE RISK INHERENT IN THE MARKET .....</b>	<b>4</b>
<b>V. CREDIT RISK .....</b>	<b>9</b>
<b>VI. FINANCIAL RISK MANAGEMENT EXECUTION .....</b>	<b>10</b>
<b>APPENDIX A: HEDGE POLICY BOARD RESOLUTION .....</b>	<b>11</b>
<b>APPENDIX B: GAS SUPPLY RISK MANAGEMENT COMMITTEE MEMBERS.....</b>	<b>13</b>
<b>APPENDIX C: CURRENTLY APPROVED FINANCIAL COUNTERPARTIES .....</b>	<b>15</b>
<b>APPENDIX D: RISK MANAGEMENT INSTRUMENT EXAMPLES.....</b>	<b>17</b>
<b>APPENDIX E: HEDGING GUIDELINES .....</b>	<b>23</b>

## **I. PROGRAM OBJECTIVES**

The objectives of Intermountain Gas Company's ("Intermountain or the Company") Gas Supply Risk Management Program ("Program") are:

- a) help insure adequate natural gas supplies, transportation and storage are available for its customers needs,
- b) to mitigate the adverse impact that significant price movements in the natural gas commodity can have on the Company's supplies, customers and other operations, and
- c) minimize the credit risk inherent in the implementation of certain price risk reducing strategies.

The measures employed in meeting these objectives include the use of operational measures as well as the effectuation of risk-reducing financial instruments.

The Program objectives acknowledge that natural gas is a commodity and that fundamental elements of a free market commodity include its price is largely influenced by actual, as well as perceived, market and supply imbalances and that its intermediate and longer term price should trade around the commodity's cost of production.

It is not the objective of this program, as more fully explained herein, to realize the lowest cost of actual natural gas purchases for delivery to its customers.

**SPECULATION IS PROHIBITED UNDER ANY CIRCUMSTANCE.** Speculation is defined as using financial instruments based on expected price trends without being matched to a physical natural gas purchase requirement.

## **II. ORGANIZATIONAL STRUCTURE**

### **A. Board of Directors**

The Board of Directors of the Company recognizes the need for management to use certain risk mitigation tools to reduce risk and its corporate governance obligation inherent in risk management. In 1995, the Board of Directors adopted by Board Resolution a Risk Management Policy dealing with Hedging that provides policy guidance to this Program. Such resolution is attached hereto as Appendix A.

## **B. President**

The President of Intermountain is responsible for the development of the strategic direction for the Company and as such is responsible for the establishment of and overseeing the structure, direction, conduct and control of the Company's Gas Supply Risk Management Program. A Gas Supply Risk Management Committee ("Committee") has been established to assist the President in these responsibilities.

## **C. Gas Supply Risk Management Committee**

The Gas Supply Risk Management Committee consists of a senior level management team (see Attachment B), established by the President, responsible for developing and implementing the Company's Gas Supply Risk Management Program. The performance of this function will include and incorporate the elements of:

- a) adequate and reliable natural gas supplies,
- b) adequate and reliable natural gas transportation and storage,
- c) customer price stability in light of the price risk inherent in the commodity markets,
- d) appropriateness and accessibility of certain risk-reducing financial instruments,
- e) credit risks inherent in the implementation of the above noted elements.

The Committee shall recognize that timely information and prompt management attention are also important elements in the realization of the Program objectives and, in that regard, the Committee will hold regularly scheduled, as well as on an as needed basis, meetings in the performance of their duties. Minutes will be kept for each meeting, which will serve as documented Committee authorizations and actions.

## **III. ADEQUATE AND RELIABLE NATURAL GAS SUPPLIES, TRANSPORTATION AND STORAGE**

To help insure that this Program objective is met, the Committee will perform an assessment of long-term (one to five year) natural gas demand, supply, transportation and storage on a regular basis. This assessment incorporates the same elements found in the Company's Integrated Resource Plan filed Bi-annually with the Idaho Public Utilities Commission. This demand forecast will be reviewed in

aggregate form as well as a Load Duration Curve that examines the daily gas requirement needs during the winter and shoulder month periods. The demand forecast will be viewed in light of the available transportation, storage, and contracted gas supply resources to identify any deficits in the available delivery or supply volumes. Supply resource deficits typically take the form of 1) base load deficits that can be supplied with annual supply contracts, 2) shoulder month deficits that can be met with a combination of storage and seasonal supply contracts, and 3) needle peaking deficits that, although generally met with storage, may or economically should require short-term or spot market purchases.

The Company may use an outside representative to help it carry out its gas supply responsibilities. Currently Intermountain has under contract, IGI Resources, Inc. ("IGI" – a BP Energy Company) who is directed by the Committee to solicit on Intermountain's behalf the necessary supply, transportation and or storage resources to meet any projected needs and deficits.

The Committee will ensure that no gas supply, transportation or storage contract, either long-term or short-term, is consummated without due diligence as to its need or the related aspects of security, reliability, credit risk and price. The Committee will recognize and place emphasis on the value in longer term contractual arrangements when implementing the Company's supply, transportation and storage portfolios and insure that these arrangements are staggered as to their renewal date in such a way as to enhance the Company's ability to renegotiate the same.

Once the supply portfolio is in place, it will then be managed on a day-to-day basis matching the supply resources to the daily needs of Intermountain's customers. The Company's Gas Control Department will provide IGI with a "one month ahead" look at its anticipated demand. This forecast will embody the aforementioned Load Duration Curve as well as, inter alia, the latest outlook for the weather. IGI will again match this shorter-term, updated demand forecast against the contracted supplies already in place to determine if existing supplies are adequate, whether or not additional short-term supplies are necessary, opportunities for off-system sales, and opportunities for short-term transportation acquisitions or releases. Additionally, a daily requirements forecast will be performed by Intermountain's Gas Control Department and transmitted to IGI at least 24 hours in advance of the gas day which will "fine tune" Intermountain's daily gas needs and incorporate the most up-to-date weather outlook.

#### **IV. MITIGATE THE ADVERSE IMPACT OF COMMODITY PRICE RISK INHERENT IN THE MARKET**

Another of the objectives of the Company's Gas Supply Risk Management Program is to mitigate the adverse impact that significant price movements in the natural gas commodity can have on the Company's customers and other operations. If, in the determination of the Committee, there is a material likelihood that projected wholesale prices will rise significantly from current levels the Committee will begin to consider the effectuation of certain risk-reducing transactions to include, but not limited to, those outlined in Appendix D attached hereto.

On a regular basis, the Committee will review the actual and anticipated natural gas commodity prices (Weighted Average Cost of Gas or "WACOG") delivered into Intermountain's system. This review will include a forecasted WACOG price for the current as well as subsequent Purchased Gas Cost Adjustment or "PGA" periods. These WACOG projections, with the assistance of IGI, will incorporate at a minimum 1) an outlook for the impact Intermountain's storage resources delivered during the winter heating season will have on the projected WACOG, 2) a point in time reference to future gas prices as predicted by the futures market for those supplies currently subjected to a market index, and 3) any natural gas supplies with a fixed price secured through the employment of various financial instruments or otherwise. The Committee will then decide upon certain risk management actions by applying its judgement, based upon, inter alia, market supply and demand fundamentals, technical trends from the trading environment and anticipated future price movements in evaluating the market risk inherent in these WACOG projections.

Natural gas is a commodity traded on the open market like other commodities such as oil, coffee or lumber. As with most commodities, natural gas prices are ultimately determined by the balance of supply and demand in a regional marketplace. When demand is high in relation to supply, natural gas prices tend to rise. When supply is high in relation to demand, prices tend to fall.

There are numerous factors that affect natural gas supply and demand. The actual supply and demand for natural gas relies on a variety of interrelated factors making it difficult to predict how these factors will combine to shape the overall supply and demand curve and resultant price.

Given the relationship between natural gas prices and the supply and demand for natural gas, Intermountain's Gas Supply Risk Management Committee looks at a variety of "fundamental natural gas supply and demand price drivers" when anticipating future natural gas prices. The more pertinent drivers are more fully delineated below. Some of these drivers impact the near term price while others can be more pertinent to longer term pricing making it even more difficult to determine reasonable price estimates beyond three years.

### **Fundamental Natural Gas Supply And Demand Price Drivers**

- **Electrical generation** - Natural gas consumed by electrical generation now rivals the residential market in size. Gas fired electric generation typically increases with summer air conditioning loads. Natural gas, which is traditionally injected into storage during the summer, now has additional summer market demand influencing its price (see "Weather"). Electric generation has, in some instances, moved the emphasis of storage injections from the middle of the summer to the more price volatile "shoulder months."
- **Snow pack/stream flow** - Lower stream flows force hydroelectric generators to seek other fuel alternatives - usually natural gas.
- **Rig counts** - A high level of natural gas rig counts will tend to offset decline curves and moderate current prices as well as futures prices as increased production is brought to market.
- **Weather** - Natural gas demand typically peaks during the coldest months and tapers off during the warmer months, with an increase during the summer to meet the demands of gas fired electric generators. The actual, as well as the anticipated, weather during any particular season can affect the cyclical price and demand for natural gas:
  - **Summer** - Warm summer weather brings with it greater cooling demands causing an increase in gas fired electric generation thereby influencing the market price of natural gas. The price for natural gas injected into storage during the summer is impacted by the level of gas consumed by electric generation.
  - **Winter** - Colder winter weather brings with it more pronounced natural gas consumption. Conversely, a warm winter results in less pronounced consumption. A significant "winter peak" depletes storage



stocks at an accelerated rate and results in a greater demand for storage injection gas in the summer.

Moderate weather for both summer and winter generally provide more stable supply and demand balance.

- **Industrial Demand** - Supply and demand in the marketplace determine the short term price for natural gas. However, this can work in reverse as well. The price of natural gas can affect its demand. This is particularly true for those consumers who have the capacity to “fuel switch.” While most residential and commercial customers rely solely on natural gas to meet many of their energy requirements, some industrial and electric generation consumers have the capacity to switch between fuels. For instance, during a period of extremely high natural gas prices, many electric generators may switch from using natural gas to using cheaper coal, thus decreasing the demand and thereby the price, for natural gas. For some industries, a sustained high price for natural gas can actually result in a permanent regional “destruction” of that demand due to plant closures or relocations.
- **Economy** - The state of the U.S. economy in general can have a considerable effect on the demand for natural gas in the short term, particularly for industrial consumers. When the economy is expanding, output from industrial sectors is generally increasing at a similar rate. When the economy is in recession, output from industrial sectors typically drops. These fluctuations in industrial output accompanying economic upswings and downturns affects the amount of natural gas needed by these industrial users. For instance, during the economic downturn of 2001, industrial natural gas consumption fell by 6 percent. Thus the short term status of the economy has an effect on the amount of natural gas consumed in the United States. Global economies can also come into play. Products manufactured in the U.S. for foreign export which include natural gas in the manufacturing process can influence the price of natural gas. The price for Liquid Natural Gas (“LNG”) imports can fluctuate with the market demands placed on LNG by other countries.
- **Natural Gas Storage Levels** - Natural gas storage facilities are a vital factor in offsetting seasonal fluctuations in demand. In summer when demand is low, natural gas is injected into storage facilities and withdrawn again during the winter when demand is high. Increased national attention has been given to “working gas in storage.” High storage levels in relation to “average”

storage levels have a dampening affect on natural gas prices and the opposite is true in relation to low storage levels.

- **Natural Gas Pipeline Grid** - The natural gas pipeline transportation infrastructure continues to expand the connection between supply basins and the consuming markets. Natural gas supplies that were once dedicated to single consuming regions are now available to multiple consuming markets through the interconnection of intra and interstate pipelines. As these interconnections continue to grow, the price paid for natural gas in Southern Idaho will increasingly mirror national price levels.
- **Financial markets** - While these markets bring important tools which help to stabilize future prices, they also have introduced speculation and its attendant volatility that can cloud the effect that physical supply and demand fundamentals should have on the pricing equation. The shrinking of trading/hedging market players has also resulted in degradation to the “liquidity” of natural gas pricing in certain markets and has also masked the pricing impact that would otherwise take place given the physical characteristics of the market.
- **Other Commodities** - The price of oil and its ability to be substituted for natural gas for energy requirements influences the price of natural gas given the dual fuel capability of many electric generation units and other industrial users.<sup>1</sup>
- **Technological and Efficiency Advancements** - In the longer term, the advancement of new and existing natural gas technologies and improvements in efficiencies will play an increasing role in the demand for natural gas. Distributed generation, for instance, offers promise in the industrial sector. The reliability and flexibility offered by the on-site generation of electricity is particularly important for the industrial sector, where loss of electricity could have negative consequences, including spoiled products for a manufacturer dependent on electricity. Advancements in the more efficient use of natural gas continues to have a dampening affect on the residential, commercial and industrial demand for natural gas.

---

<sup>1</sup> Additionally, the market has begun to correlate movements in oil prices to movement's in natural gas prices and, in so doing, changes to NYMEX oil prices have begun to influence even our regional natural gas prices.

- **LNG** - The pricing for this form of natural gas is increasingly subjected to global influences like crude oil is today. This will add volatility and additional risk when predicting prices beyond three years.
- **World events** - World events, such as conflict in oil-producing regions and growing energy demand from developing countries, can influence the price of crude oil. This in turn influences the price of natural gas as industries switch between fuels, driving up the demand for natural gas.<sup>2</sup>

Again, it is very difficult to predict how these factors will combine to shape overall demand and therefore influence price. A study of these fundamentals will, however, be used on a regular basis to influence Intermountain's Gas Supply Risk Management Committee when applying its judgment as to price direction and in evaluating the market risk inherent in certain WACOG projections. In conjunction with the application of these supply and demand fundamentals as well as other judgmental applications, the Committee will also overlay historical prices onto these projected prices as an added measure in determining the potential for future significant price changes.

This Program and its Committee shall recognize that any decision by an entity as to fixing or not fixing the purchase price of its natural gas requires the exercise of considerable judgment. The decision to fix represents the entity's belief that prices are going to or likely will rise significantly in the future and protection against such a rise is desired. It can also represent the entity's desire to stabilize prices against possible future price increases at a level that is considered workable in a particular circumstance. The Committee must always remember that the ability to enter into fixed price arrangements means the counterparty (selling party) believes the price of the commodity is going to move in the opposite direction that the buying party believes the commodity will move. In other words, any entity that enters into a fixed price transaction must understand and accept the fact that the very next day and every day thereafter the decision to fix the price will likely prove to be incorrect (positively or negatively). That is why, in part, it is not an objective of this Program to realize the lowest price for its purchase requirements.

Notwithstanding the above, the Committee is authorized to effectuate risk-reducing transactions in an effort to mitigate the impact of significant price movements and thereby stabilize customer prices. The application of these transactions will

---

<sup>2</sup> Additionally, the market has begun to correlate movements in oil prices to movements in natural gas prices and, in so doing, changes to NYMEX oil prices have begun to influence even our regional natural gas prices.

consider the overall fundamentals inherent in commodity pricing, and be directed towards, 1) the volatility inherent in each of the Company's supply basins and, 2) the volatility inherent in the natural gas commodity purchasing "seasons". In other words, application of certain risk reducing transactions may be supply basin and season specific.

The application of these risk-reducing transactions may be triggered by the real or anticipated availability in the futures market of certain fixed price targets, established by the Committee in the application of the above mentioned evaluations. The Committee will effectuate the application of certain risk management transactions when and if the futures market affords the Committee the option of fixing its un-hedged gas supplies at a price at or near those gas prices currently embedded within the approved tariffs of the Company. The Committee will also apply its judgment in determining what portion, if any, of its overall supply needs should then be risk management transacted when and if these price targets materialize in the marketplace. Additionally, the Committee will use its judgment as to the type of risk management tool or product to utilize in the application of these transactions. Appendix E more specifically describes the Committee's hedging guidelines.

IGI will supply regular reports to the Committee that summarize existing financial positions as well the corresponding WACOG for a given PGA period(s).

## **V. CREDIT RISK**

Credit Risk for the Company and its customers will be defined for the purposes of this Risk Management Program as:

- a) the uncertainty that a counterparty to a hedging transaction will be able to fulfill its present and future financial obligation under that transaction and,
- b) the extent to which the Company's existing credit capacity might be constrained do to the incremental borrowing requirements (margin calls) brought on by either rising natural gas prices or the failure of a hedging counterparty to fulfill its contractual obligation.

The credit risk of each counterparty to a transaction will be researched by the Company's Treasury Department and reported to the Committee. The Committee will then determine the appropriateness of consummating a financial transaction with those counterparties given the reported risk and recommend measures to

mitigate any risk delineated by the Treasurer's Report which the Committee feels can be rectified.

The Treasury Department shall also report to the Committee what the "in or out of the money" status is on existing financial contracts as well as perform "stress tests" or functionally equivalent tests to measure the possible credit capacity requirements of existing or contemplated transactions.

## **VI. FINANCIAL RISK MANAGEMENT EXECUTION**

Intermountain will execute risk-reducing financial transactions pursuant to Hedge Policy authority provided by Board Resolution and as directed by the Committee only through its outside representative, IGI. IGI will then provide all trade documentation in a form satisfactory to the Company.

Risk-reducing financial instruments will include, but may not be limited to, Over the Counter ("OTC") financial instruments, as approved by the President for use by the Committee. Examples of certain financial instruments available for the Committee's consideration and use are outlined in Appendix D hereto. The market parameters inherent in these instruments will be regularly reviewed by the Committee in helping to determine the appropriateness of their use. The Committee may also recommend that additional risk-reducing financial instruments be considered. By the approval of the President, such additional risk-reducing financial instruments may be employed by the Committee.

The Committee will approve financial counterparty criteria. The selection criteria used to evaluate the attractiveness of potential and existing counterparties will include credit risk, derivative pricing, quality of execution, margin requirements, "back office" support, reliability, account executive, and confidentiality. Multiple counter parties may be desirable. Appendix C hereto provides a list of currently approved financial counterparties.

**APPENDIX A**  
**HEDGE POLICY BOARD RESOLUTION**

