



## **Administrative Report**

### **Office of the Director of Financial Services/Treasurer**

**To:** Warden McNamara and Members of County Council

**From:** Sandra Zwiers, MAcc, CPA, CA  
Director of Financial Services/Treasurer

**Date:** Wednesday, October 07, 2020

**Subject:** Electricity and Natural Gas Update – Commodity  
Price Hedging Strategy – AMO/LAS

**Report #:** 2020-1007-FIN-R015-SZ

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#### **Purpose**

The purpose of this report is to provide Council with an update on the Corporation's utilization of commodity price hedging and recommend continued participation with the Association of Municipalities of Ontario / Local Authority Services Ltd (AMO/LAS) Procurement Programs, to procure, in bulk, electricity and natural gas in the open market on behalf of partnering municipalities.

#### **Background**

In accordance with the Municipal Act, 2001, regulation 653/05, and the County of Essex Commodity Price Hedging Policy (Policy 06-11), the Treasurer is required to report annually on all commodity price hedging agreements in place. The goal of the commodity price hedging policy is to allow the Treasurer to enter into fixed price agreements for the future delivery of all or any portion of a commodity when deemed advantageous to do so.

The County continues to utilize the services of AMO/LAS Procurement Programs. As part of the strategy, a hedging contract is used to minimize potential risk of spot market fluctuations.

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A hedge is a financial agreement that fixes the price to be paid by the municipality for future delivery of a commodity. A hedge is typically used to reduce cost fluctuations and provide cost certainty.

The County's current agreement with LAS includes a hedge of 50% of its total electricity requirements. This hedging level has been in place since the last report to County Council in October of 2017. The hedge is applicable to all electricity purchased by the Corporation with the exception of street light usage which is kept on the spot market. Because street light energy demand typically occurs during off-peak/lower cost times, the benefit of hedging is low.

For natural gas, LAS purchases incremental gas contracts at various points each year with a goal of building a total hedge portfolio of 80-90% of program requirements for the current year, with the remaining consumption settling at prevailing market rates.

## **Discussion**

### **Electricity**

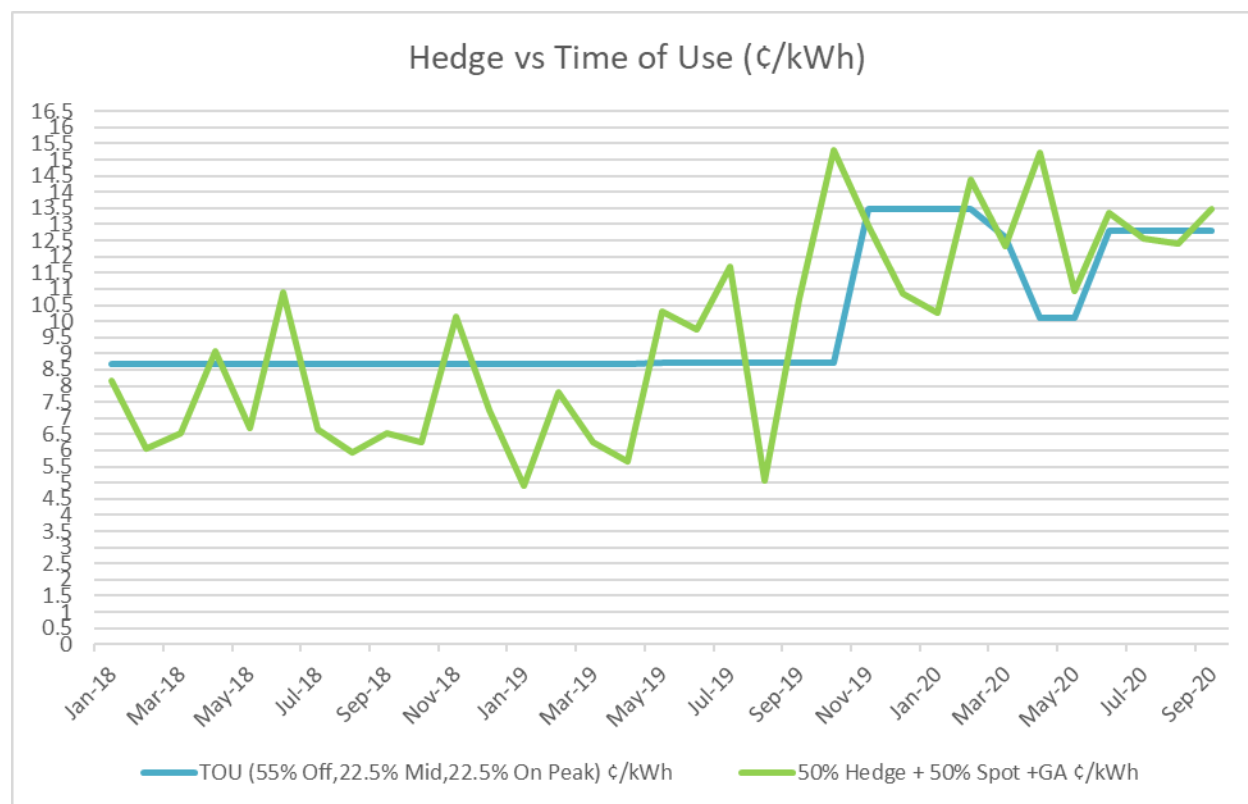
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The Corporation's electricity bills consist of a number of cost components:

- Energy Charge (based on actual usage and set by retailer)
- Global Adjustment Charge (set by province)
- Delivery Charge (set by regulation)
- Regulatory Charges (set by regulation)

The only component of the bill that is eligible for hedging is the energy charge. All other components of the bill are regulated and ineligible for hedge protection.

The graph in Table 1 illustrates the hedging results for the Corporation for the period January 1, 2018 to present 2020. For the majority of the reporting period, the Corporation's 50% hedging strategy has resulted in energy charge savings over the time of use rates.

**Table 1 – Electricity Hedging Results (2018 – Present)**

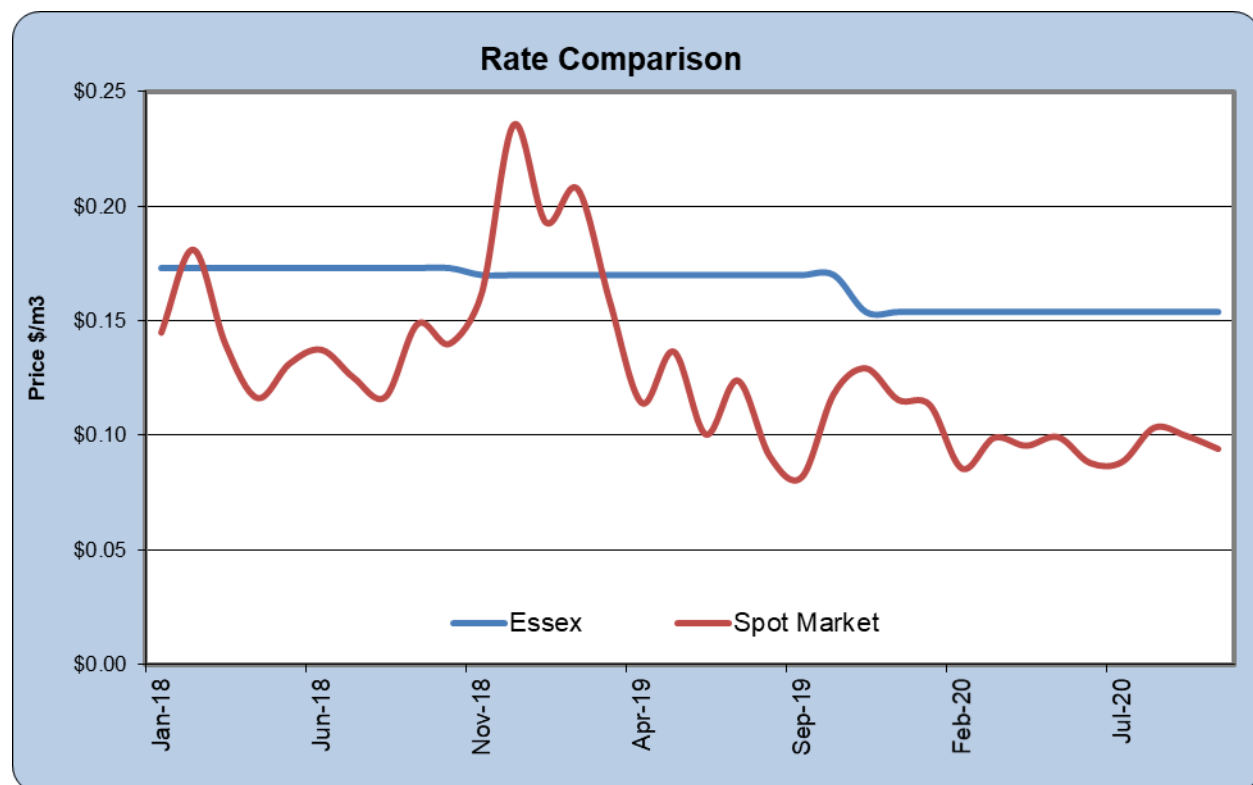
## Natural Gas

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The hedging program for natural gas includes a rebate feature that returns program savings back to participating municipalities. In 2018 and 2019, the Corporation received rebate payments in the amount of \$10,184 and \$13,306 respectively.

In terms of the components of the natural gas bill that are eligible for hedging, the program offers pricing stability for the commodity charge as well as the deregulated transportation charges. All other components of the natural gas bill are regulated and ineligible for hedging.

The graph in Table 2 illustrates the stability offered by the hedging program for the period from January 1, 2018 to present 2020. The program is designed to provide rate stability rather than guarantee rate savings.

**Table 2 – Natural Gas Hedging Results (2018 – Present)**

While commodity prices in the day markets and short term have remained relatively stable/low since mid-2019 and into 2020 due to ample supply, the future market outlook is expected to be far more volatile. Natural gas storage is currently above the five-year average and analysts question whether the low pricing currently being experienced is sustainable into 2021. It is anticipated that the hedging rate will more closely approximate market rates, if not fall below market rates, into next year.

## **Financial Implications**

The goal of participating in the LAS hedging programs is to ensure stable commodity rates to assist in annual budgeting. The high level of regulation in the commodity markets does admittedly have a limiting effect on any hedging program.

## **Recommendation**

That County Council receive the report on Commodity Price Hedging Strategy as information.

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Respectfully Submitted

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Originally Signed by

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Concurred With,

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