

Clarke-Mobile Counties Gas District -- Black Belt Energy Gas District

ANPR on Physical Commodities Activities of FHCs (Docket No. R-1479)

On July 10, 2014, Sheldon Day, Al Bean, and Jim Choukas-Bradley, representing the Clarke-Mobile Counties Gas District and the Black Belt Energy Gas District (the "Districts"), met with Scott Alvarez, General Counsel and Michael Waldron, Special Counsel. They expressed concern that any steps discussed in the ANPR that would lead to the inability of FHCs to participate in the market for long-term natural gas supplies purchased through gas prepayment transactions would adversely affect the Districts and the members of the public that they serve. The Districts are municipal-owned public corporations formed under Alabama law that provide natural gas distribution and sales services and operations and business support expertise to residential, commercial and industrial customers as well as other municipal gas systems and joint action agencies. The Districts believe that FHCs help provide an essential component of their supply portfolio, namely long-term prepaid gas supply transactions. They believe that the departure of FHCs from the natural gas market would curtail or end their ability to engage in these important transactions in the format that best meets their needs, and they do not believe that the risks cited in the ANPR are sufficient to justify restrictions that would end FHC involvement in these transactions.

The attached handout was also provided.

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**Clarke-Mobile Counties Gas District –  
Black Belt Energy Gas District**

**Meeting with Scott Alvarez, General Counsel  
Board of Governors of the Federal Reserve System**

**Concerning the Federal Reserve's Advance Notice of Proposed  
Rulemaking, Docket No. 1479 and RIN 7100 AE-10**

**July 10, 2014**

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**Mayor Sheldon Day**  
Mayor of Thomasville, Alabama  
Chairman of the Board of Directors  
Clarke-Mobile Counties Gas District and Black Belt Energy  
Gas District  
Thomasville, Alabama

**Al Bean**  
Co-General Manager  
Clarke-Mobile Counties Gas District and Black Belt Energy  
Gas District  
Jackson, Alabama

**Jim Choukas-Bradley**  
Legal Counsel  
McCarter and English, LLP  
Washington, D.C.



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## CMC and BBE: Essential Points

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- We represent Clarke-Mobile Counties Gas District and Black Belt Energy Gas District, two municipally-owned gas companies, who are buyers and sellers of natural gas to residential and industrial consumers.
- There are hundreds of rural communities like us with the same interests and obligation to deliver gas to our consumers at all times, no matter how cold the winter.
- For almost a decade, we have relied on FHCs and other major banks for the physical supply of natural gas through natural gas prepayment transactions.



## Clarke-Mobile Counties Gas District: Organization and Service Area

- Clarke-Mobile Counties Gas District (“CMC”) is a public corporation formed by the southwest Alabama cities of Jackson, Grove Hill and Thomasville on April 2, 1953, under Act No. 762, General Laws of Alabama (the “Gas Districts Act”).
- CMC’s mission is to utilize a highly trained and knowledgeable staff to provide safe and reliable delivery of natural gas service to Residential, Commercial and Industrial customers in Clarke, Mobile, Washington, Baldwin, Choctaw, Escambia and Wilcox Counties.
- CMC is governed by a three member Board of Directors consisting of the Mayors of Jackson, Grove Hill and Thomasville.
- CMC serves approximately 6,500 Residential and Commercial customers through 172 miles of transmission lines and 452 miles of distribution lines. Our services impact directly and indirectly over 500,000 people each year.
- Pursuant to CMC’s Certificate of Incorporation, CMC also sells gas wholesale to other publicly-owned natural gas distribution systems for consumption in the service areas of those systems and to large industrial natural gas customers.



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## Black Belt Energy Gas District: Organization and Service Area

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- Located in Jackson, Alabama; Black Belt Energy Gas District (“BBE”) was established in August 2008 as a public corporation and gas supply district under the Gas Districts Act. BBE is governed by a three-member Board of Directors comprised of the Mayors of Thomasville, Jackson and Grove Hill.
- The mission of BBE is to serve as the natural gas supply acquisition arm of CMC and provide natural gas supply, operations and business support expertise to other public gas entities, both inside and outside the state of Alabama.
- Associated Municipal Alliances:  
Clarke-Mobile Counties Gas District; Lower Alabama Gas District; Louisiana Municipal Gas Authority; Southeast Gas Acquisition & Supply Association; Florida Gas Utilities; Municipal Gas Authority of Georgia; Tennessee Energy Acquisition Corporation; American Public Gas Association
- Strategic Efforts:  
Developing natural gas prepayment transactions; supplying prepaid natural gas volumes to the Louisiana Municipal Gas Authority (LMGA), with 70+ municipalities across Louisiana; currently providing Residential and Large Industrial customer consulting and operational services to municipalities in Alabama, Louisiana, Florida and Georgia.



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## CMC and BBE MISSIONS

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■ **CMC/BBE Core Focus: Safe, reliable delivery of natural gas to our customers at competitive, reasonable, and affordable prices**

■ **Focus Tiers:**

■ 1<sup>st</sup> is a safe delivery pipeline infrastructure:

Follow all DOT PHMSA Regulations and Guidelines

■ 2<sup>nd</sup> is immediate reliability of supply:

Important for daily and seasonal customer needs

■ 3<sup>rd</sup> is long-term reliability of supply:

Important for potential industrial customers locating in our communities

■ 4<sup>th</sup> is competitively priced supply:

Important in maintaining existing industrial customers in our communities

■ **Risks factors associated with acquiring natural gas supply:**

■ Market risk: Can be managed by hedging

■ Transaction risk: Can be managed somewhat; a counterparty's ability to execute is a factor

■ Counterparty risk: The financial security and credit quality of counterparties in the over-the-counter and physical markets are crucial



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## CMC and BBE: Counterparty Risk

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### ■ CMC/BBE Ranking of Counterparty Risk:

- Exchange traded instruments for immediate reliability of supply
  - Safest counterparty
  - Transparent
  - Trade is backed by the exchange
  - Counterparty maintenance easy
  - But daily margining requirements can be a hit to cash flow
- Physical purchases for immediate to 18-month reliability of supply
  - Trades are handled through a NAESB contract
  - No margining
  - Adequacy of credit is crucial to security of supply
    - Smaller marketers may not have adequate lines of credit to cover their natural gas cost in a rising market. This is a factor that does not surface until there is a drastic market move up and the marketer cannot make natural gas deliveries.
    - FHCs have strong credit and the parents' balance sheet contains no more than 5% investment in commodities, so there is far less concern about the ability to perform.



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## CMC and BBE: Counterparty Risk (continued)

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### ■ CMC/BBE Ranking of Counterparty Risk:

- Over-the-counter transactions for long-term reliability of supply: 1 to 30 years

#### ■ Energy Traders

- Trades are done through an ISDA Contract
- Currently limited to 10 years
- Trade is backed by the trading subsidiary
- Counterparty maintenance is a challenge
- Margining requirements are not necessarily on a daily basis

#### ■ FHCs

- Trades are done through an ISDA Contract
- Currently can transact up to 30 years
- Trade can be backed by the parent
- Counterparty maintenance can be less challenging
- Because an FHC is governed under the Bank Holding Company Act such that the FHC must comply with the rules around complementary activities in trading physical commodities, the FHC is a stronger counterparty in the over-the-counter market.
- FHCs and other major banks are the most important and most viable natural gas prepayment counterparties, and under current market conditions are the only viable counterparties.

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## CMC and BBE: Long-Term Prepaid Natural Gas Supply Purchases

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- Pursuit of long-term gas prepayment transactions is the number one supply priority for BBE and CMC.
- These transactions bring reliable long-term supplies at prices discounted to market prices and are essential to economic development and the growth and stability of our gas districts.
- Prepayment transactions since 2006 have only been completed with FHCs and other major banks.
- BBE is close to completion of a major gas prepayment transaction with one FHC.
- BBE is in discussions with other FHCs concerning its next prepayment transactions after that one.
- Marketers and producers are not participants in the 15-, 20-, and 30-year prepayment markets.
- CMC has been a project participant in four successfully completed gas prepayment transactions since 2006 and is a potential project participant in three others.
- These transactions have translated into industrial recruitment and lower rates to gas consumers



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## Role of the Gas Districts in the Natural Gas Industry

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- Business relationships with gas suppliers:
  - Natural gas marketing companies
  - Gas producers
  - Energy affiliates of major banks
- Business relationships with interstate pipelines
- Business relationships with intrastate pipelines
- Business relationships with local gas producers
- Business relationships with other gas distribution systems
- Business relationships with gas storage companies
- Business relationships with governmental joint action agencies



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## CMC and BBE: Conclusions

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- We believe the FHCs to be contributors to a balanced, reliable and transparent natural gas market.
- Prepaid gas supply transactions and fixed-price transactions with FHCs are essential components of our supply portfolio.
- Given current rules under the BHC Act, as we understand them, regarding complementary commodities activities which:
  1. Prevent FHCs from dominating the Natural Gas Market and
  2. Preclude FHCs from participating in the Natural Gas Industry's riskier activities,

There is no compelling reason to remove FHCs from the physical natural gas commodity markets.



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## Appendix 1 - CMC and BBE: Representatives

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### ■ Mayor Sheldon Day, Thomasville, Alabama

- Former Walmart manager and mayor for 18 years, serving 5<sup>th</sup> term
- Longest-serving president of CMC and Chairman of BBE
- Recruited \$700 million in outside investment and created 1,500 direct new jobs in a city with population of 5,000
- Active in the political and economic development of the region at the state, national and international levels

### ■ Al Bean, Co-General Manager of CMC and BBE

- 30 years of experience in the natural gas industry
- 15 years of experience in distribution and operations
  - Career-long familiarity with pipeline safety, best practices and compliance with state and federal guidelines
- 15 years of experience in gas hedging and gas supply
- American Public Gas Association Board member and former president of Alabama Natural Gas Association

### ■ Jim Choukas-Bradley, Legal Counsel

- Representing municipal gas systems since 1980
- Leading practitioner in helping public gas systems operate from the fully regulated to the deregulated natural gas industries



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## Appendix 2 - CMC and BBE: Business Relationships with FHCs

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**Bank of America** – BBE has pursued prepayment transactions with B of A. CMC is a participant in a prepayment transaction undertaken by another joint action agency with B of A affiliate Merrill Lynch Commodities Inc. under which CMC continues to receive gas deliveries.

**Barclays Bank PLC** – Barclays is BBE's commodity swap counterparty in the pending J. Aron/Goldman prepayment transaction.

**Citigroup Inc.** – BBE and CMC have pursued prepayment transaction discussions with Citigroup.

**Credit Suisse** – Credit Suisse was the commodity swap counterparty in two prepayment transactions with Societe Generale in which CMC was a participant.

**DeutscheBank** – DeutscheBank was the prepaid gas supplier in the pending Tenenergy prepayment transaction, in which CMC is a participant.



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## Appendix 2 - CMC and BBE: Business Relationships with FHCs (continued)

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**Fortis** – BBE and CMC’s Financial Advisor has met with Fortis concerning potential prepayment transactions.

**Goldman Sachs** – BBE has a gas prepayment transaction with J. Aron & Company and The Goldman Sachs Group pending, awaiting improvement in market conditions. CMC is a participant in a gas prepayment transaction undertaken with J. Aron/Goldman by another joint action agency and is receiving deliveries of gas from that transaction.

**JPMorgan** – CMC is a participant in a prepayment transaction with JPMorgan undertaken by another joint action agency and continues to receive gas deliveries from it. JPMorgan is the BBE swap counterparty in another gas prepayment transaction in which CMC is a participant.

**Morgan Stanley** – BBE has pursued prepayment transaction discussions with Morgan Stanley.



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## Appendix 2 - CMC and BBE: Business Relationships with FHCs (continued)

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**Royal Bank of Scotland** – BBE has pursued commodity swap counterparty discussions with RBS.

**Societe Generale** – CMC was a participant in both the Lower Alabama Gas District prepayment transaction with Soc Gen and the Southeast Alabama Gas District prepayment transaction with Soc Gen.

**UBS AG** – CMC pursued participation in a Florida Gas Utility prepayment project with UBS.

**Wells Fargo** – BBE pursued direct prepayment transaction discussions with Wells Fargo over an extended period of time, as well as indirect discussions through participation in the PEAK Sooner prepayment transaction with Wells Fargo. BBE continues to pursue prepayment opportunities with Wells.

