GUAM POWER AUTHORITY
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June 12, 2013

Mr. Frederick J. Horecky, Esq.
Administrative Law Judge
Public Utilities Commission
643 Chalan San Antonio, Suite 102B
Tamuning, Guam 96913

SUBJECT: GPA Docket 10-03 Fuel Hedging Program
Ref: GPA Status Report on the Implementation of the New Fuel Hedging Protocol

Dear Judge Horecky:

In connection with the order of the Public Utilities Commission (PUC) dated March 26, 2012, the Guam Power Authority (GPA) wishes to discuss the actions taken to develop the new Fuel Hedging protocol.

While we acknowledge there have been some delays on GPA's part, we also believe there has been some misunderstanding regarding the complexity of the transition to the new protocol. As the PUC is aware, the new protocol expands GPA's ability to utilize different hedge products. Prior to approval of the new protocol, GPA was only allowed to conduct hedge transactions utilizing no cost collars. Under the new protocol, GPA is allowed to enter into the purchase of call options, the sale of put options, various combinations of the two, monetize gains, purchase swaps for the current market price of GPA's fuel. The protocol does not put a cap on the amount of fuel to be hedged in a single month or period. The implementation of such significant changes to GPA Hedging program requires some time for a transition.

After the Fuel Hedging protocol was approved by the PUC, GPA went back to the Consolidated Commission on Utilities (CCU) to gain approval. The Fuel Hedging protocol that had been adopted by the PUC was very different from the protocol that had been reviewed and approved by the CCU earlier.

After approval of the program was received, GPA went back to the CCU for approval to create a Risk Management Committee. The new protocol calls for the establishment of this high level committee in the organization. This approval was received.

After receiving approval to establish the Risk Management Committee, GPA started looking for resources concerning the Risk Management Committee. GPA had never had a Risk Management Committee before and no one in management at GPA had ever seen a Risk Management Committee in effect. GPA decided to retain Baker Tilly for the purpose of assisting with the establishment of the committee.

GPA also flew one of its key personnel to Washington, D.C. to go through additional training regarding the rollout of the new program. One of the recommendations that came out of that training was for the consultant that developed the Fuel Hedging protocol to come out to GPA to perform one final training session for all of the parties that will be involved in the Fuel Hedging protocol.

GPA has also continued to input the daily spot market price and forward curves into the Fuel Hedging model and has used the results to develop a few hedge transactions.

In the last hedge transaction, GPA was unable to locate its hedge contacts in a timely manner when the model indicated a trade was warranted. Additional data and prices are needed to determine the optimal hedging product once the model signals that an action is required. GPA has learned that it needs contact information from the trading desks of its hedge providers so as to get up to the minute data before a hedge product can be purchased. Because of this, GPA has lost a couple of trading opportunities but GPA believes it is part of a learning curve that must occur before a program of this complexity can be initiated.

With regards to the items specifically enumerated in the LEAC Order in GPA Docket 12-13, dated - January 29, 2013, PUC, GPA makes the following responses:

(i) to provide the required and appropriate human resources needed to execute GPA's hedging needs,

GPA Response: The hedging protocol also requires that there be a segregation of duties in place to perform hedge transactions. GPA has not had sufficient personnel to allow for this segregation of duties. I have authorized the Finance Department to add one additional personnel for this purpose and that hiring process is currently ongoing. GPA has also developed some Standard Operating Procedures (SOPs) for the Fuel Hedging program to ensure all parties are aware of their responsibilities.

(ii) demonstrate that its hedging personnel are properly trained on the use its hedging model and hedging instruments available in the market,

GPA Response: GPA has been trying to identify a time for the final training session to take place, however, because we are so close to hiring the person whose main responsibility it will be to operate the program, we decided it would be best to wait till the person comes on board to have the training.

(iii) the retaining of an independent party to "shadow" GPA activities until GPA demonstrates it has adequate internal resources in place and has mastered the hedging model,

GPA Response: GPA had retained Scientific Applications International Corporation (SAIC) for the purpose of conducting this training and plans to utilize the consultant to "shadow" GPA for the early transactions and then to perform periodic audits of the Fuel Hedging program. Unfortunately, at the time the Fuel Hedging protocol was approved, GPA was nearing the contractual cap for its contract with SAIC. GPA issued a new Request for Proposals for this purpose. SAIC was again selected as the most responsible vendor and GPA is again working with SAIC to implement this program.

(iv) inclusion in its hedging program the option for GPA to hedge 100% of its fuel requirement to maximize price protection to consumers and prevent margin calls on GPA,

GPA Response: As mentioned in the second paragraph, this is allowed by the protocol.

(v) file fuel hedging reports with the PUC with the existing LEAC regulatory reporting which should include a calculation of Value at Risk (VaR).

GPA Response: Please refer to Exhibit A – GPA VaR

The transition towards implementation of the new Fuel Hedging protocol has not been as timely as we would have wanted. We would have wanted to be at full implementation by this time, however, at the same time, a program with this level of complexity is not something we want to rush to create. We want to make sure our staff is fully trained and capable before we fully implement the new protocol.

Some of the comments that have been made at PUC meetings where this has been discussed seem to indicate that GPA has done nothing to implement the protocols. We wanted to take this opportunity to explain all the steps that have been taken towards full implementation of the program. We are working very hard to have a full implementation of the new protocol in the very near future.

Sincerely,

Joaquin C. Flores, P.E.
General Manager

cc: Mr. Graham Botha, Legal Counsel
Mr. Randall V. Wiegand, CFO
GM CFO 017 13

Exhibit A - GPA VaR

Value at Risk Report

Confidential Information
Date of Evaluation: 06/11/2013
Using Prices as of Close of: 06/10/2013

	Volumetric Needs	Needs Hedged	Market Prices	Previous Hedge	Previous Hedge Price	Portfolio Price	Mark to Market	Cost at Market	Cost at Portfolio	Upside VaR ($)	Downside VaR ($)
	MT	*MT*	*$/MT*	*%*	*$/MT*	*$/MT*	*$/MT Favorable / (Unfavorable)*	*$*	*$*	*$*	*$*
Jul-13	35,476	10,000	$ 610.00	28%	$ 636.15	$ 617.37	$ (7.37)	$ 21,640,423	$ 21,901,923	$ *1,321,539*	$ *518,737*
Aug-13	33,756	10,000	$ 606.50	30%	$ 635.10	$ 614.97	$ (8.47)	$ 20,472,783	$ 20,758,783	$ 2,025,949	$ 852,829
Sep-13	34,320	-	$ 605.25	0%		$ 605.25	$ -	$ 20,772,021	$ 20,772,021	$ 5,502,569	$ -
Oct-13	34,396	-	$ 602.95	0%		$ 602.95	$ -	$ 20,738,767	$ 20,738,767	$ 6,448,005	$ -
Nov-13	32,412	-	$ 602.95	0%		$ 602.95	$ -	$ 19,542,626	$ 19,542,626	$ 7,009,419	$ -
Dec-13	33,749	-	$ 602.95	0%		$ 602.95	$ -	$ 20,348,970	$ 20,348,970	$ 8,170,159	$ -
Jan-14	34,599	-	$ 601.05	0%		$ 601.05	$ -	$ 20,795,566	$ 20,795,566	$ 9,014,916	$ -
Feb-14	31,141	-	$ 601.05	0%		$ 601.05	$ -	$ 18,717,022	$ 18,717,022	$ 8,838,440	$ -
Mar-14	34,477	-	$ 601.05	0%		$ 601.05	$ -	$ 20,722,417	$ 20,722,417	$ 10,482,122	$ -
Apr-14	33,365	-	$ 597.85	0%		$ 597.85	$ -	$ 19,947,185	$ 19,947,185	$ 10,372,700	$ -
May-14	34,477	-	$ 597.85	0%		$ 597.85	$ -	$ 20,612,091	$ 20,612,091	$ 11,382,830	$ -
Jun-14	33,773	-	$ 597.85	0%		$ 597.85	$ -	$ 20,191,188	$ 20,191,188	$ 11,805,262	$ -

Notes:
VaR is a statistical metric that estimates the potential unfavorable movement of prices given a chosen confidence level and time. For GPA the VaR is to expiration and with a 95% confidence level
Upside VaR represents the potential cost in addition to the current "Cost at Portfolio" if prices continue to rise and there is no incremental hedge takes place
Downside VaR represents the potential opportunity cost in addition to the current mark-to-market if prices deteriorate significantly and no incremental hedge takes place