Seattle City Light

Memorandum

DATE: February 21, 2013

TO: Mayor Michael McGinn
Seattle City Council

FROM: Jorge Carrasco

SUBJECT: Financial Update – December 2012

This memo provides an analysis of Seattle City Light's financial condition and operating results through December 31, 2012. The attached Income Statement Analysis, which is summarized in the chart below, provides a summary of how City Light performed in 2012 compared to 2011 and the 2012 Financial Plan. The 2012 Financial Plan is based on the revenues and expense projections included in the adopted budget for 2012.

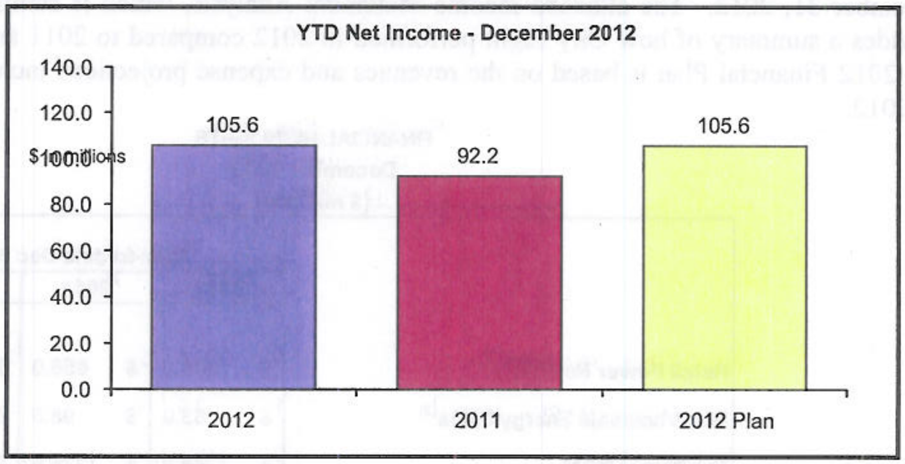
FINANCIAL HIGHLIGHTS
December 2012
($ millions)

	Year-to-date Dec 31		
	2012	**2011**	**Plan**
Retail Power Revenues(1)	$ 664.3	$ 656.0	$ 677.5
Net Wholesale Energy Sales(2)	$ 63.9	$ 98.5	$ 102.1
Net Power O&M	$ (245.2)	$ (226.6)	$ (253.8)
Net Non-Power O&M	$ (188.2)	$ (188.2)	$ (210.5)
RSA Transfers, Net(3)	$ 13.2	$ (62.2)	$ (1.1)
Taxes, Depreciation & Other	$ (202.4)	$ (185.3)	$ (208.5)
Net Income	**$ 105.6**	**$ 92.2**	**$ 105.6**
Operating Cash	$ 156.3	$ 155.4	$ 163.4
Construction Account - Restricted	$ 106.1	$ 61.5	$ -
Rate Stabilization Account(4)	$ 128.3	$ 141.5	$ 113.8
Bond Reserve(5)	$ 34.2	$ 34.2	$ 3.7
Other Restricted Assets	$ 7.2	$ 4.7	$ 4.4
Total Cash	**$ 432.1**	**$ 397.3**	**$ 285.3**
Debt Coverage Ratio	1.81	1.84	1.80
Debt to Capitalization Ratio	**62.8%**	**64.0%**	**61.8%**

(1) Retail Power Revenues include revenues such as Green Power Program and Power Factor Charges and exclude low-income Rate Discounts.
(2) Revenue from wholesale sales, before booked out long term purchases.
(3) Transfers from the RSA less transfers to the RSA.
(4) Reflects a transfer of $40.5 million and $22 million from operating cash into Rate Stabilization Account at the end of 2011 and 2012, respectively.
(5) Funds from the Surety Bond Replacement Fund were moved to the Bond Reserve Account on June 1, 2012.

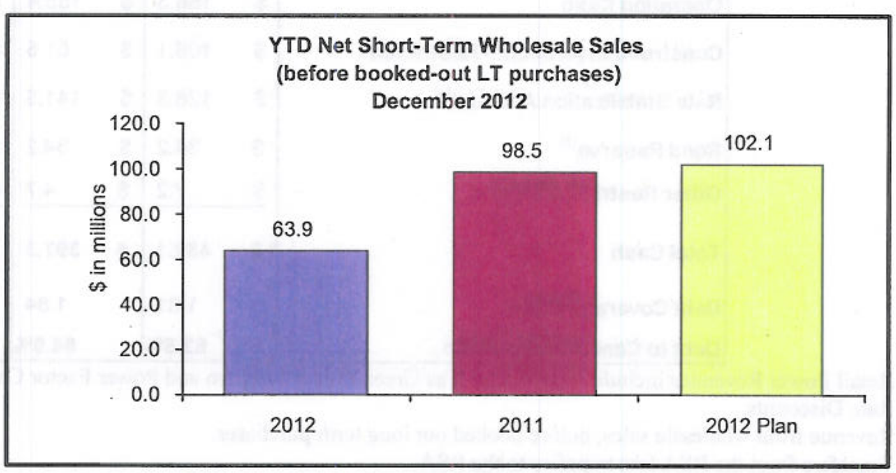
Net Income

As indicated in the table on the previous page and in the chart below, net income for 2012 was $105.6 million, which is a $13.4 million or 14.5% increase over 2011. This increase is driven by higher retail power revenues due to the across-the-board 3.2% rate increase effective January 1, 2012, lower BPA expenses and lower customer service expenses due to lower bad debt expense. Offsetting factors include higher administrative and general expenses, lower power-related revenues and lower capital grants. In addition, both in 2011 and 2012 City Light's management made a decision at year-end to transfer cash that would result in an estimated 1.85x debt service coverage ratio from the operating account into the RSA. However, in 2012 transfers from the RSA were larger than transfers to the RSA due to lower than planned net wholesale revenues.



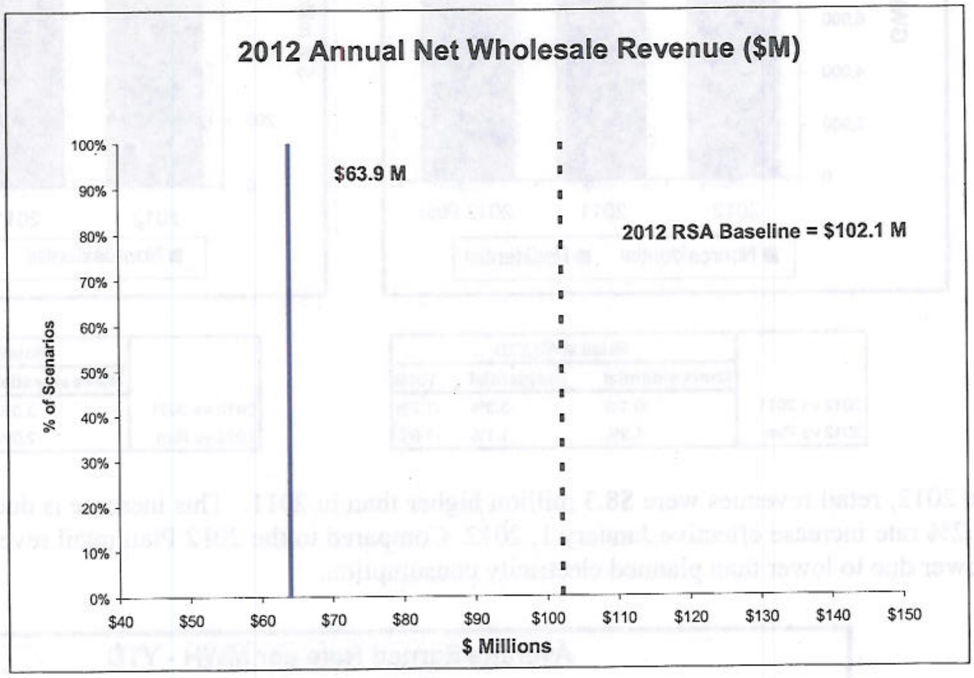
Actual 2012 net income was the same as in the 2012 Financial Plan. As indicated in the Financial Highlights table on page 1, both revenues and expenses were lower than planned. The Net Income Variance Analysis attached to this letter provides more detail.

Net Short-Term Wholesale Energy

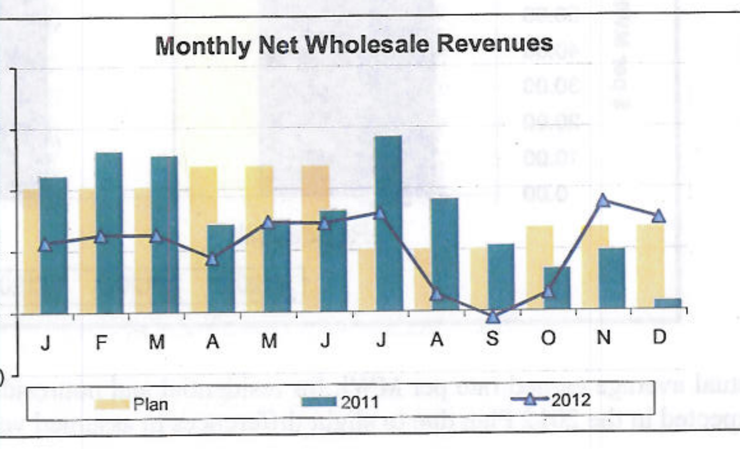


The chart below compares 2012 actual net short-term wholesale revenues before booked-out long-term purchases, which totaled $63.9 million, to the $102.1 million RSA baseline amount projected in the 2012 Financial Plan.

The 2012 planned net wholesale revenue is calculated as specified by RSA Ordinance 123260 and is an average of the historical sales. Therefore, it does not reflect current market conditions. The actual net wholesale revenue is based on much lower energy prices than the historical average and lower energy surplus available for sale.

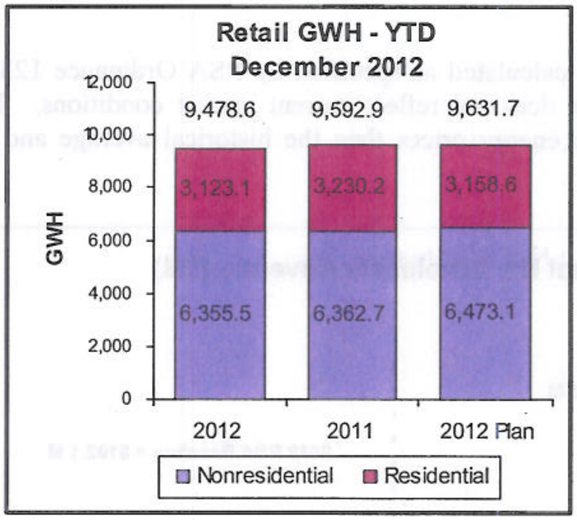


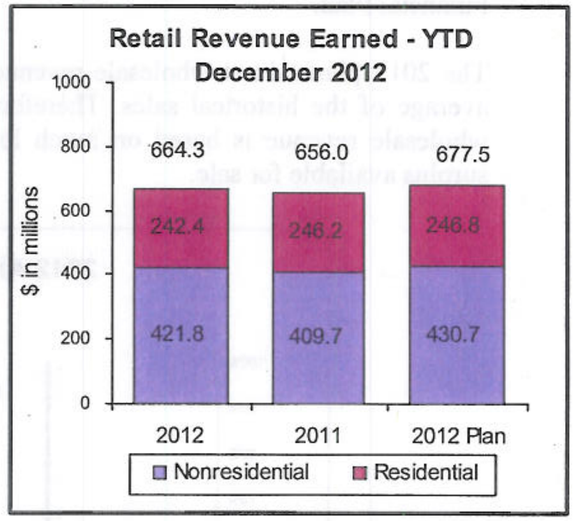
Net wholesale revenues in December 2012 were $7.5 million, $6.7 million higher than in December 2011. The primary driver of this increase was much higher surplus this December as compared to last. The prices in December 2012, however, were lower than in December 2011.



Retail Power Revenues

The charts that follow present selected data on year-to-date retail power revenues.

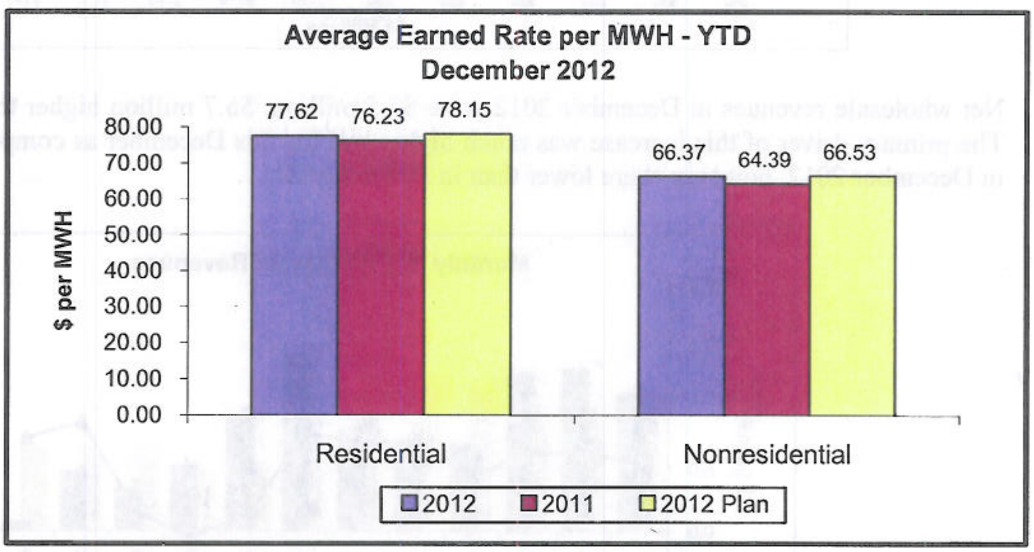




	Retail MWh YTD		
	Nonresidential	Residential	Total
2012 vs 2011	-0.1%	-3.3%	-1.2%
2012 vs Plan	-1.8%	-1.1%	-1.6%

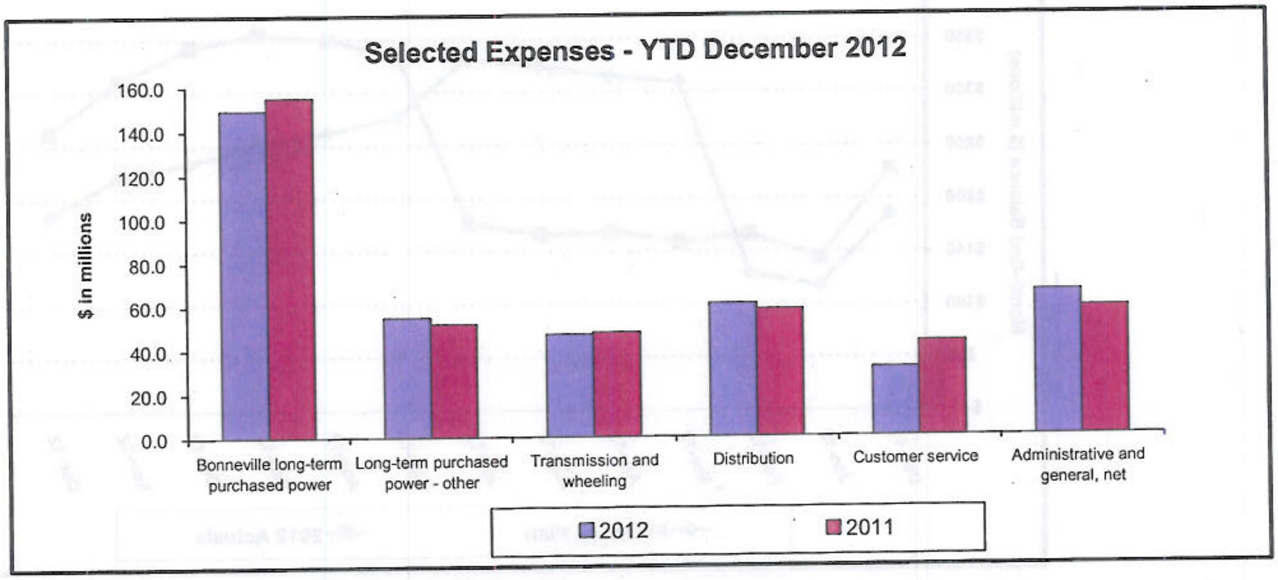
	Retail Revenue YTD		
	Nonresidential	Residential	Total
2012 vs 2011	3.0%	-1.6%	1.3%
2012 vs Plan	-2.0%	-1.8%	-2.0%

In 2012, retail revenues were $8.3 million higher than in 2011. This increase is due to the across-the-board 3.2% rate increase effective January 1, 2012. Compared to the 2012 Plan retail revenues were $13.2 million lower due to lower than planned electricity consumption.



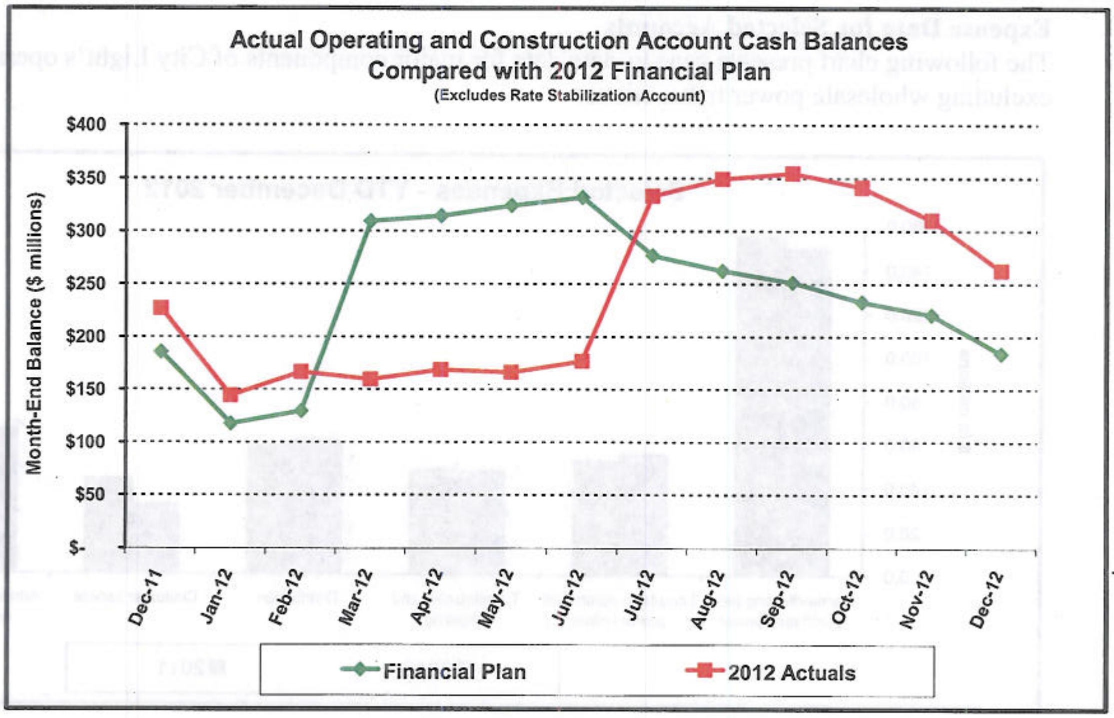
The actual average earned rate per MWh for residential and nonresidential customers is different from what was expected in the 2012 Plan due to slight differences in assumed versus actual patterns of consumption.

Expense Data for Selected Accounts
The following chart presents year-to-date data for major components of City Light's operating expenses excluding wholesale power transactions.



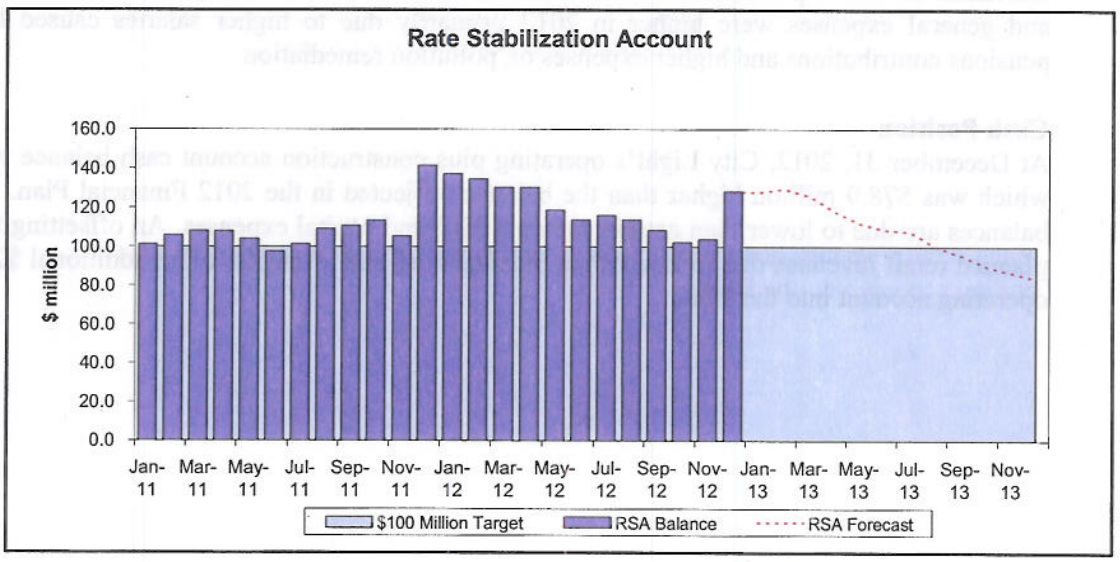
Bonneville expenses were lower in 2012 than in 2011 due to lower BPA slice purchases. Offsetting factors are lower BPA Slice true-up credit and higher BPA block purchases. Long-term purchased power expenses were higher in 2012 primarily due to higher purchases from GCPHA and Stateline Wind projects. Transmission expenses were slightly lower in 2012 than in 2011 due to a reassignment of transmission costs for the Lucky Peak project to the buyer in 2012. Distribution expenses were higher in 2012 because of increased efforts dedicated to inspection and replacement of overhead and underground distribution lines. Customer service expenses were much lower in 2012 due to lower expense for bad debt. Administrative and general expenses were higher in 2012 primarily due to higher salaries caused by COLAs, higher pensions contributions and higher expenses on pollution remediation.

Cash Position
At December 31, 2012, City Light's operating plus construction account cash balance was $262.4 million, which was $78.9 million higher than the balance projected in the 2012 Financial Plan. These higher cash balances are due to lower than anticipated operating and capital expenses. An offsetting factor is lower than planned retail revenues due to lower than planned load and a transfer of an additional $22 million from the operating account into the RSA.



RSA Position

The cash balance in the RSA was $128.3 million as of December 31, 2012. The chart below shows that during 2012 the Department has been transferring funds from the RSA to supplement lower than expected Net Wholesale Revenues ($38.2 million). The increase in December 2012 reflects a transfer of $22 million from the operating account into the RSA. Looking forward City Light does not expect a RSA surcharge in 2013.



2012 Budget
City Light was within its budget authority in 2012 and there were no legal budget exception for any Budget Control Level. The Department has spent 90% of the overall O&M budget (O&M budget includes Non-Power O&M expenses, Purchased Power, Taxes and Debt Service) through year-end. The significant areas of under-expenditure include lower purchased power costs and salary savings from vacant positions. City Light's spending on the Capital program through December is 92% of the 2012 work plan. The majority of this variance resulted from rescheduling of work associated with InterAgency projects. Excluding InterAgency, the rest of City Light's spending was 97% of the 2012 work plan.

Debt-to-Capitalization
At December 31, 2012, City Light's debt-to-capitalization ratio was 62.8%, slightly higher than the 2012 Plan of 61.8% but a decrease from 64.0% reported at December 31, 2011.

Compliance with Risk Policies and Standards
Attached for your information is the City Light Risk Oversight Status Report as of December 12, 2012, which conveys City Light's compliance with risk policies and standards at that point in time.

Performance Metrics
In addition to the financial information included above, we have provided a report on performance metrics for Distribution Operations, Vegetation Management, Safety and Human Resources, Power Resources and Customer Care. The updated Performance Metrics Report for December 2012, with 2011 data included for comparison, is attached.

Attachments

Line No.	Condensed Statements of Revenues and Expenses	Year-to-date [A] Actuals December 31, 2012	[B] Actuals December 31, 2011	[A - B] Actuals to Actuals Variance	Year Ending December 31, 2012 [D] 2012 Financial Plan	[A - D] Variance
1	Unaudited					
2	In millions					
3						
4						
5	**Operating Revenues**					
6	Retail power revenues	$ 664.3	$ 656.0	$ 8.3	$ 677.5	(13.2)
7	Short-term wholesale power revenues, net (lines 41 + 44)	70.4	102.7	(32.3)	146.1	(75.7)
8	Power-related revenues - other	29.3	54.6	(25.3)	35.9	(6.6)
9	Transfers from/(to) rate stabilization account	13.2	(62.2)	75.4	(1.1)	14.3
10	Other revenues	23.1	20.4	2.7	22.2	0.9
11	Total operating revenues	800.3	771.5	28.8	880.6	(80.3)
12	**Operating Expenses**					
13	Generation	32.3	29.3	3.0	39.1	(6.8)
14	Bonneville long-term purchased power	149.3	155.1	(5.8)	150.8	(1.5)
15	Long-term purchased power - other	54.8	51.8	3.0	65.8	(11.0)
16	Short-term wholesale power purchases	11.8	11.4	0.4	49.1	(37.3)
17	Power-related wholesale purchases - other	7.8	9.0	(1.2)	7.3	0.5
18	Other power costs	10.3	10.2	0.1	11.8	(1.5)
19	Transmission and wheeling	47.0	47.9	(0.9)	49.0	(2.0)
20	Distribution	60.9	58.3	2.6	68.0	(7.1)
21	Customer service	31.3	43.2	(11.9)	36.7	(5.4)
22	Conservation	20.7	19.1	1.6	27.7	(7.0)
23	Administrative and general, net	66.1	58.7	7.4	61.4	4.7
24	Taxes	74.9	73.6	1.3	77.6	(2.7)
25	Depreciation and amortization	94.8	90.4	4.4	89.7	5.1
26	Total operating expenses	662.0	658.0	4.0	733.8	(71.8)
27						
28	**Net Operating Income**	**138.3**	**113.5**	**24.8**	**146.8**	**(8.5)**
29						
30	**Other Deductions, Net**					
31	Investment Income	5.2	4.9	0.3	5.4	(0.2)
32	Other income (expense), net	4.7	7.4	(2.7)	5.7	(1.0)
33	Interest expense	(77.2)	(75.9)	(1.3)	(100.4)	23.2
34	Noncapital grants	2.8	1.4	1.4	3.9	(1.1)
35	Capital contributions	31.0	29.1	1.9	43.7	(12.7)
36	Capital grants	0.8	11.8	(11.0)	0.5	0.3
37	Total other deductions, net	(32.7)	(21.3)	(11.4)	(41.2)	8.5
38						
39	***Net Income***	**105.6**	**92.2**	**13.4**	**105.6**	**0.0**
40	Note A:					
41	Short-term wholesale energy sales, gross	75.7	109.9	(34.2)	151.2	(75.5)
42	Short-term wholesale energy purchases	(11.8)	(11.4)	(0.4)	(49.1)	37.3
43	**Net ST wholesale sales before booked-out LT purchases**	**63.9**	**98.5**	**(34.6)**	**102.1**	**(38.2)**
44	Booked-out long term purchases	(5.3)	(7.2)	1.9	(5.1)	(0.2)
45	Net short-term wholesale energy sales	**58.6**	**91.3**	**(32.7)**	**97.0**	**(38.4)**
46	Note B:					
47	Power-related revenues, net (line 8 minus line 17)	21.5	45.6	(24.1)	28.6	(7.1)

Net Income Variance Analysis
December 2012

Variance Year-to-Date 2012 Compared to 2011 Actuals: $13.4 million or 14.5%

Major components ($ millions):

$92.2	Net Income YTD through December 31, 2012
$8.3	Higher retail revenues due to 3.2% rate increase effective January 1, 2012
($34.6)	Lower net surplus energy sales due to lower energy surplus and lower energy prices
$75.4	RSA deferred revenues transferred-in variance
($24.1)	Lower power-related revenues, net, reflects $22.0 million lower cash revenue and $2.1 million lower noncash revenue (primarily fair valuation of power exchanges)
$5.8	Lower BPA purchased power
$11.9	Lower customer service expenses due to lower bad debt expense
($7.4)	Higher A&G, net
($4.4)	Higher depreciation and amortization
($11.0)	Lower capital grants (no land grant for wildlife conservation from State of WA)
($6.5)	Other (net)
$105.6	Net Income YTD through December 31, 2012

Variance 2012 Actuals Compared to Financial Plan: $0.0

Major components ($ millions):

$105.6	Net Income YTD through December 31, 2012 - Actuals
($13.2)	Lower retail revenues due to lower than planned load
($38.2)	Lower net surplus energy sales than planned
$14.3	Transfer from RSA to offset lower net surplus energy sales
$6.8	Lower generation expenses
$11.0	Lower long-term purchased power-other
$7.1	Lower distribution expenses
$7.0	Lower conservation expenses
($5.1)	Higher depreciation and amortization
$23.2	Lower interest expense due to a different amortization schedule of discounts and premiums on debt expense in the 2012 Plan
($12.7)	Lower capital contributions
($0.2)	Other (net)
$105.6	Net Income YTD through December 31, 2012 - Revised Forecast

Net Income Variance Analysis
December 2012

Variance Year-to-Date 2012 Compared to 2011 Actuals: $13.4 million or 14.5%

Major components ($ millions):

$92.2	Net Income YTD through December 31, 2012
$8.3	Higher retail revenues due to 3.2% rate increase effective January 1, 2012
($34.6)	Lower net surplus energy sales due to lower energy surplus and lower energy prices
$75.4	RSA deferred revenues, transferred-in, net
($24.1)	Lower power-related revenues, net, reflects $22.0 million lower cash revenue and $2.1 million lower noncash revenue (primarily fair valuation of power exchanges)
$5.8	Lower BPA purchased power
$11.9	Lower customer service expenses due to lower bad debt expense
($2.0)	Higher A&G, net.
($4.4)	Higher depreciation and amortization
($11.0)	Lower capital grants (no land grant for wildlife conservation from State of WA)
($6.[illegible])	Other (net)
$105.6	Net Income YTD through December 31, 2012

Variance 2012 Actuals Compared to Financial Plan: $0.0

Major components ($ millions):

$105.6	Net Income YTD through December 31, 2012 - Actuals
($12.2)	Lower retail revenues due to lower than planned load
($58.2)	Lower net surplus energy sales than planned
$[illegible]	Transfer from RSA to offset lower net surplus energy sales
$6.8	Lower generation expenses
$11.9	Lower long-term purchased power-other
$2.1	Lower distribution expenses
$7.0	Lower conservation expenses
($3.1)	Higher depreciation and amortization
$23.2	Lower interest expense due to a different amortization schedule of discounts and premiums on debt expense in the 2012 Plan
($12.7)	Lower capital contributions
($0.2)	Other (net)
$105.6	Net Income YTD through December 31, 2012 - Revised Forecast

City Light Risk Oversight Status Report
As Of
Wednesday, December 12, 2012

Summary

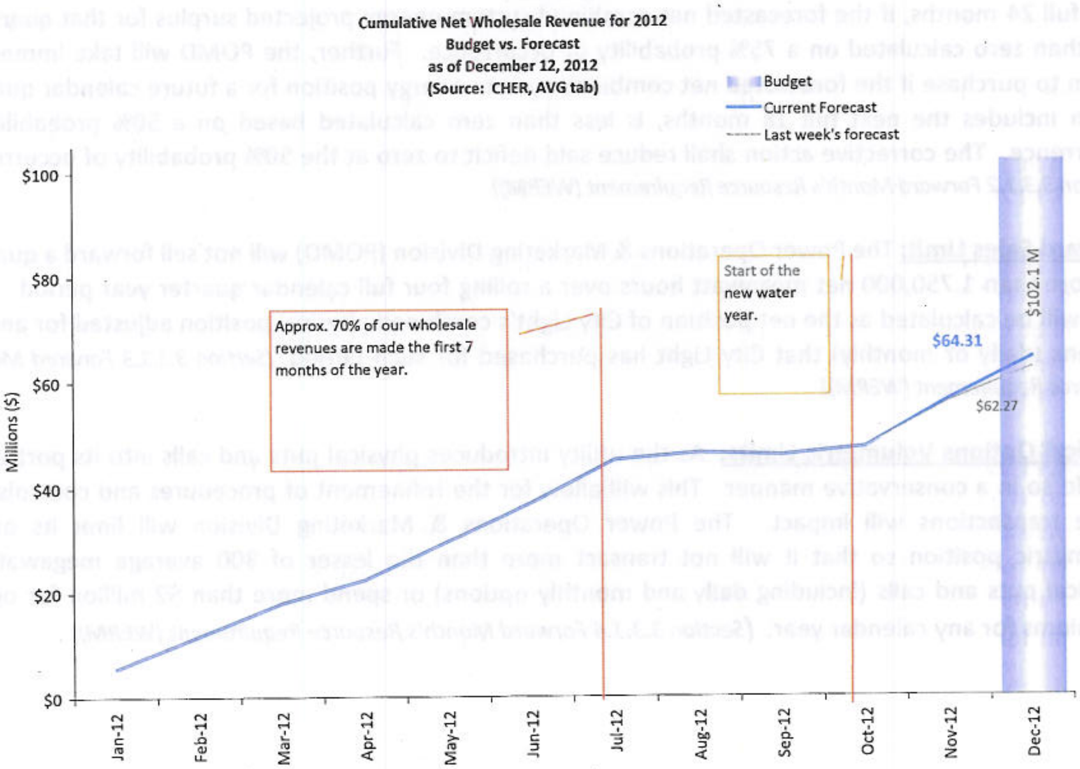
	% of 5 yr Avg	Current '12 Avg	5 Yr Avg
SCL Hydro Generation	101%	1,131 MW	1,115 MW
Peak Market Prices	52%	$23.08	$44.47

SCL Hydro Generation: The total average generation per hour for Seattle City Light's three major hydroelectric resources (Skagit, Boundary, and BPA Slice) for the 2012 calendar year. This average includes actual generation for past months, and forecasted MW for future months. The 5 year average value is comprised of actuals for years 2007-11.

Peak Market Prices: The average peak market price for the nearest electricity trading hub (Mid-C) for the 2012 calendar year. The 2012 average is comprised of monthly peak forward marks for future months and averaged Dow Jones firm peak index daily prices for past months. The 5 year average is calculated using Dow Jones peak daily prices for years 2007-11.

Wholesale Revenue Variance: As of November 30, 2012 the Net Wholesale Revenue (NWR) stands at $57.5 million. Chart 1 below compares the 2012 annual approved NWR budget of $102.1 million with the latest NWR forecast of $64.3. The NWR forecast increased by $2 million from the previous forecast of $62.27 million as a result of increase in resources. This will be the last forecast for 2012. The next report will begin reporting 2013.

Chart 1



Published Date: 12/18/12

Policy Compliance:

Tail Risk Limit	Prompt Month & Within Month Limit	Forward Month's Resource Requirement Limit	Forward Sales Limit	Physical Options Limit
Compliant	Compliant	Compliant	Compliant	Compliant

Tail Risk: For the current calendar year, the Power Operations & Marketing Division (POMD) will conduct its hedging activity to maintain the Utility's position within an $8 million Risk Tolerance Band (RTB) around the calculated 5% Tail Risk metric. For the prompt year (the year immediately following the current calendar year), the Utility's position will remain within a $10 million RTB around the 5% Tail Risk metric. *(Section 3.3.2 Prompt and Within the Month (WERM))*

Prompt Month & Within Month Volumetric Limit: The Power Operations & Marketing Division (POMD) will maintain City Light's power portfolio position for any prompt month or any Balance of the Month period so that such position shall not exceed a 50 average megawatt deficit during such period. Such limit will be calculated as the net position of City Light's combined physical position adjusted for any call options (daily or monthly) that City Light has purchased for such month. If this limit is exceeded, the Division will take immediate action to reduce the deficit to under 50 average megawatts. *(Section 3.3.1.1 Prompt and Within the Month (WERM))*

Forward Month's Resource Requirement Limit: The Power Operations & Marketing Division (POMD)will immediately suspend any further forward sales for any future calendar quarter, which includes the next full 24 months, if the forecasted net combined system energy projected surplus for that quarter is less than zero calculated on a 75% probability of occurrence. Further, the POMD will take immediate action to purchase if the forecasted net combined system energy position for a future calendar quarter, which includes the next full 18 months, is less than zero calculated based on a 50% probability of occurrence. The corrective action shall reduce said deficit to zero at the 50% probability of occurrence. *(Section 3.3.1.2 Forward Month's Resource Requirement (WERM))*

Forward Sales Limit: The Power Operations & Marketing Division (POMD) will not sell forward a quantity of more than 1,750,000 net megawatt hours over a rolling four full calendar quarter year period. Such limit will be calculated as the net position of City Light's combined physical position adjusted for any call options (daily or monthly) that City Light has purchased for such period. *(Section 3.3.1.3 Forward Month's Resource Requirement (WERM))*

Physical Options Volumetric Limits: As the utility introduces physical puts and calls into its portfolio it will do so in a conservative manner. This will allow for the refinement of procedures and controls that these transactions will impact. The Power Operations & Marketing Division will limit its option volumetric position so that it will not transact more than the lesser of 300 average megawatts in physical puts and calls (including daily and monthly options) or spend more than $2 million for option premiums for any calendar year. *(Section 3.3.1.4 Forward Month's Resource Requirement (WERM))*

5% Tail Risk Metric, 2012

In October 2007, City Light implemented a risk metric named the "5% Tail Risk". It is calculated as the average of the worst-case scenarios for City Light's cash from operations for the calendar year. Cash from operations is a bottom-line financial metric defined as the cash available to finance capital projects. There are numerous drivers of cash from operations such as retail revenue, investment income, debt service, and O&M expenses; however wholesale energy revenue is typically the primary driver of uncertainty in this metric.

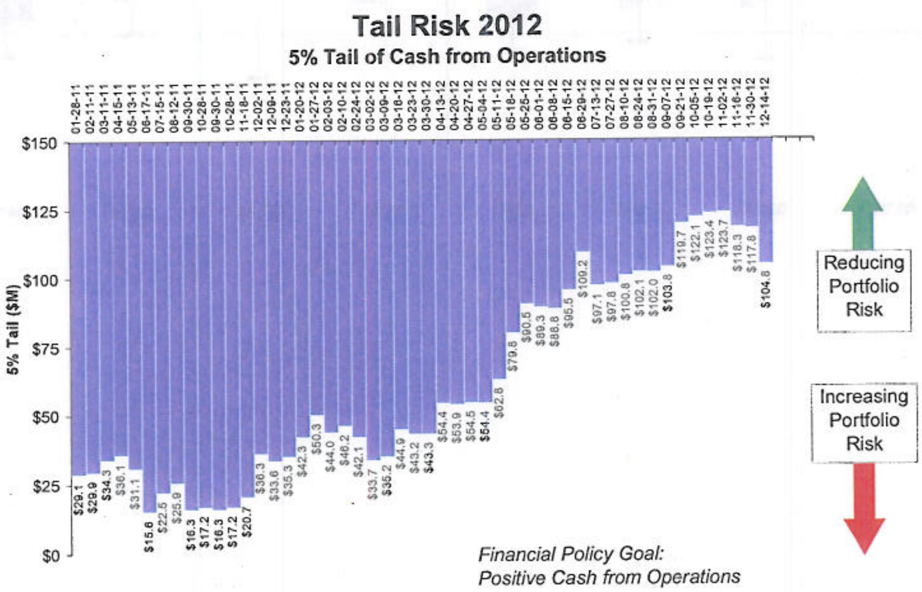
In 2011, the Rate Stabilization Account (RSA) became operational. The RSA is a cash reserve that is used to buffer the Utility from uncertainty in wholesale energy revenue. If the RSA becomes depleted, it is replenished via retail rate surcharges. The RSA significantly mitigates City Light's financial (i.e. cash from operations) risk associated with wholesale energy revenue; however retail customers are exposed in part to the wholesale energy revenue risk via RSA surcharges of up to 4.5%. To appropriately encourage management of risk borne by both City Light and retail customers, the cash from operations amount used in the 5% Tail Risk calculation excludes any effects of the RSA.

The 5% Tail Risk metric is used as a risk control measure in City Light's management of surplus hydro resources. It is used in concert with additional volumetric limits, as well as expert knowledge and analysis of western wholesale energy markets, river flow data, and generation unit outages, to inform power management decisions.

Every week, portfolio models are updated with the most current information and the 5% Tail Risk is recalculated for both the current portfolio (forecast position plus purchases, less sales) and planned portfolio (current portfolio plus remainder of existing hedge plan). The metric provides an indication as to whether the utility's portfolios include too much or too little surplus resources.

Chart 2 (below) illustrates the 5% Tail Risk metric values for the calendar year 2012. During the course of the year, the 5% Tail Risk metric value has decreased from an initial projection of $20.7 million to the current projection of a worse case of $104.8 million of Cash from Operations.

Chart 2

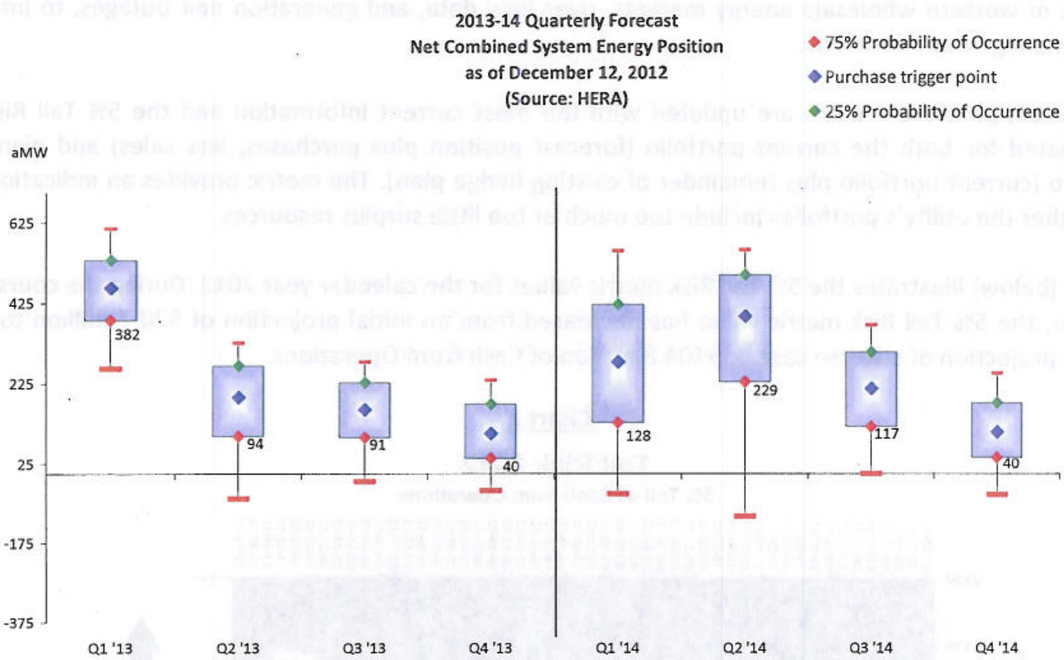


Hedging Plan & Position Status

Hedge Plan 2012, Phase 4 was last proposed and approved by the Risk Oversight Council on September 17, 2012.

Risk Policy Section 3.3.1b was amended by the Chair of the Energy and Environment Committee on March 8, 2010, changing the trigger point for purchasing power in the forward quarter-year periods to the 50th percentile (previously, it was the 25th percentile, or 75% confidence), when, at that level of expectation, the net position is below zero . On April 6, 2011, City Light's contracting authority was approved from 18 months to 24 months. Chart 3 shows the Net Combined System Energy Position for the next 8 quarter, 2 year periods to cover the full amount of City Light's contracting authority. The blue boxes represent the expected net energy position from the 25th to the 75th percentile. The dark blue diamonds inside the boxes represent the 50th percentile (the new purchase trigger). Under the amended rule, if the blue diamond is below zero, City Light must purchase energy to get back above zero.

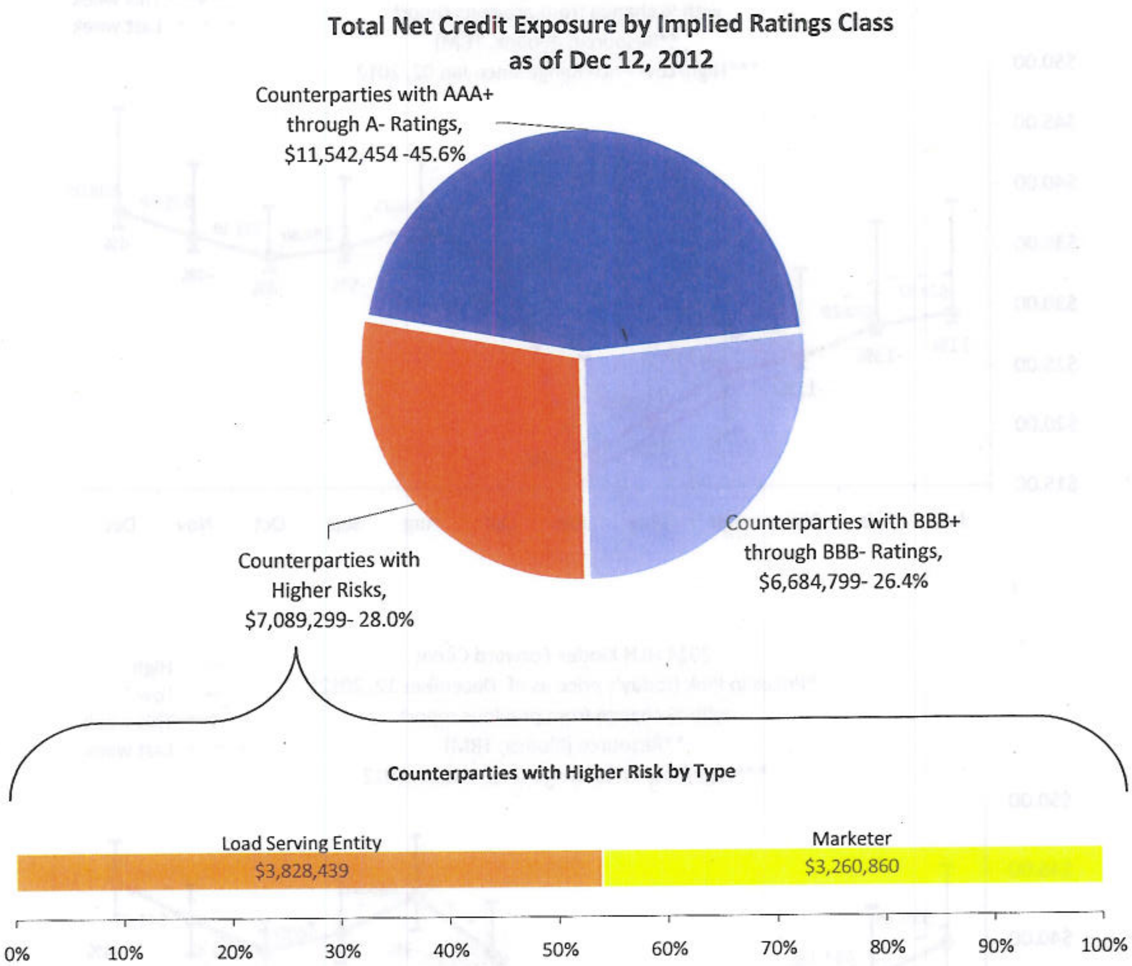
Chart 3



Credit

City Light actively manages its wholesale energy market credit risk by: setting credit limits for each counterparty that are derived from credit scoring models and analysis; securing credit enhancements; monitoring industry news; and by tracking counterparty credit exposures. Beginning in 2009 the Risk Management Division began using an industry standard tool (Moody's KMV) to proactively measure changes in counterparty creditworthiness. This necessitated the use of implied (internal) credit ratings instead of the actual rating agency ratings for Chart 4, below. It is important to note that this represents the assessment of credit risk by the Director of Risk Management. Actual credit ratings by Standard and Poor's and Moody's Investor Services are higher.

Chart 4



Credit Notes:

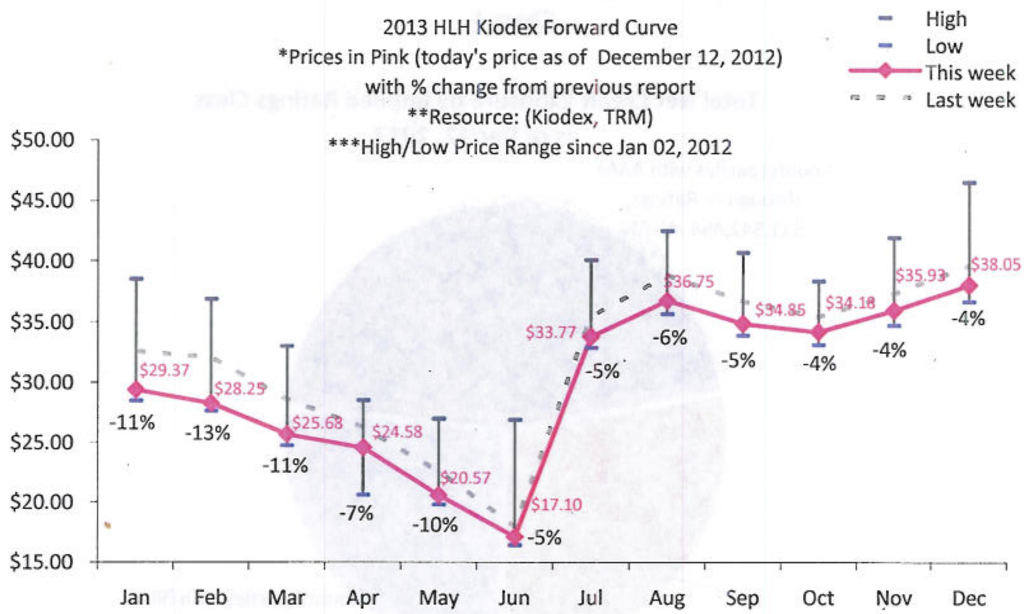
Due to recent marketing activities, Risk Oversight has temporarily increased credit for Iberdrola (PPMI) and TransAlta for real-time and day-ahead.

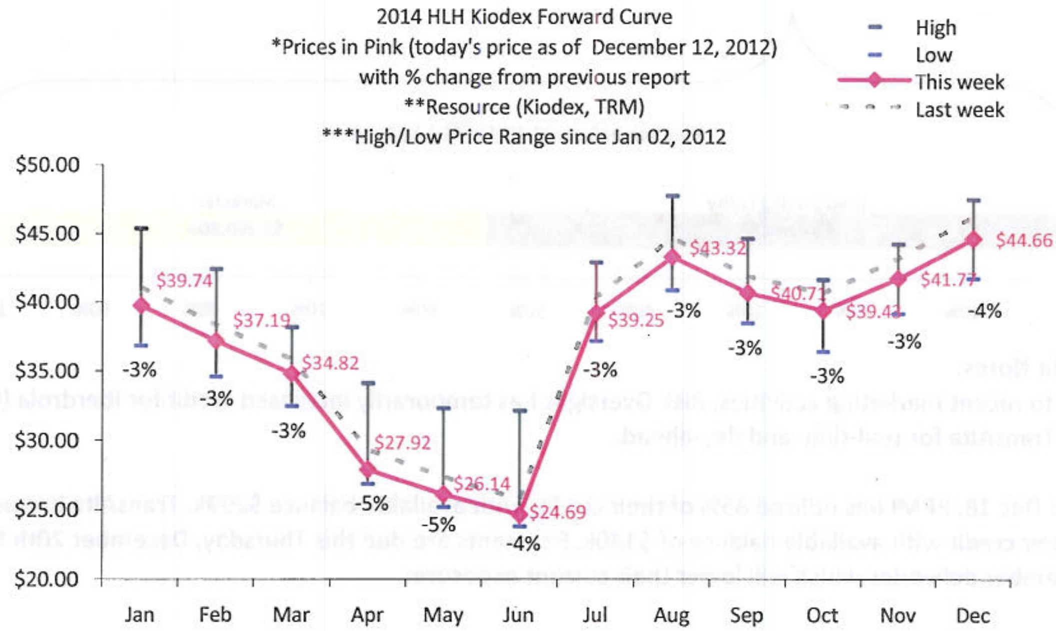
As of Dec 18, PPMI has utilized 85% of their credit, with available balance $299k. TransAlta has used 93% of their credit with available balance of $140k. Payments are due this Thursday, December 20th for November deliveries which will lower their current exposures.

Price

To ensure that prices are independently developed, City Light's official forward price curve is prepared by KIODEX and used for internal analysis, valuation and modeling tasks. Chart 5 shows the forward price range (Mid-C HLH only) for calendar year 2013 and 2014. Overall, forward prices has dropped an average of 7% for 2013 and 4% for 2014 from the last run.

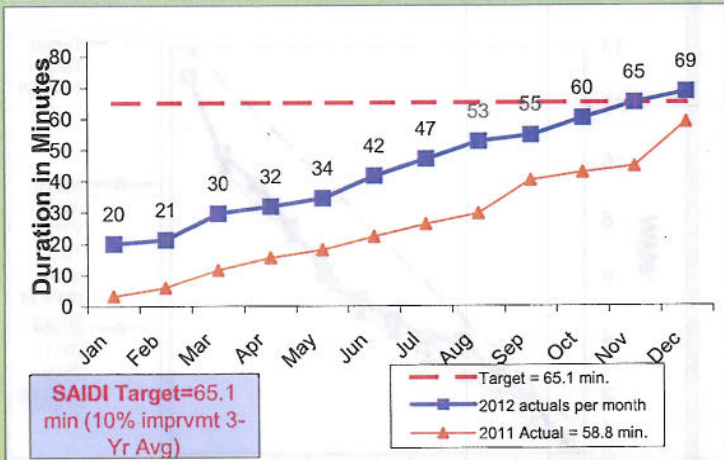
Chart 5



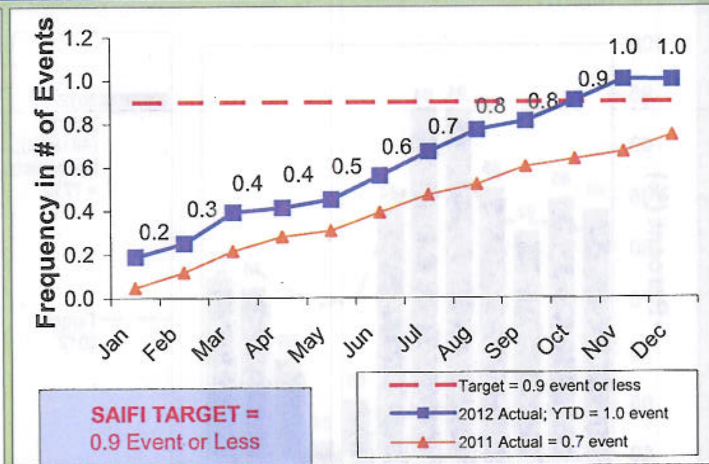


Distribution Operations:

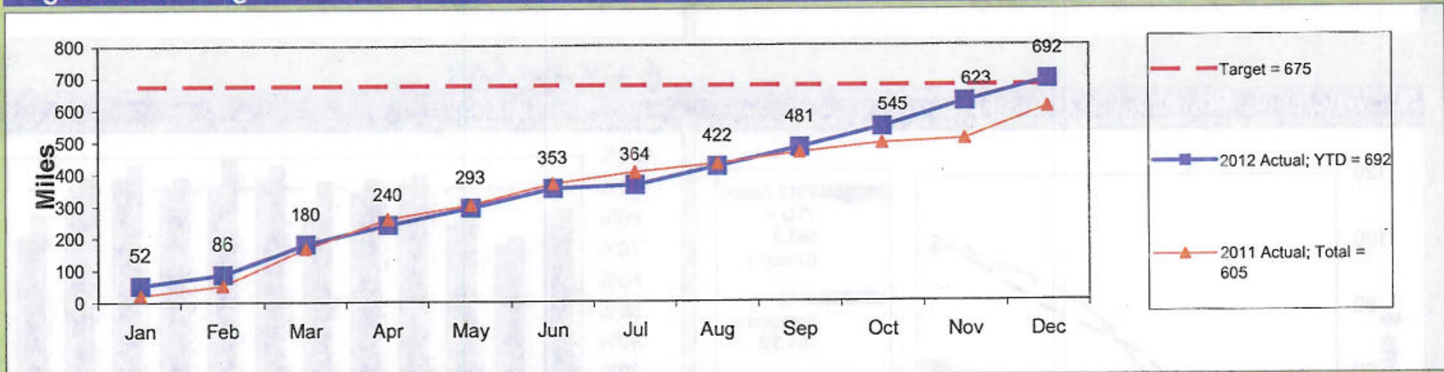
SAIDI - Cumulative



SAIFI - Cumulative

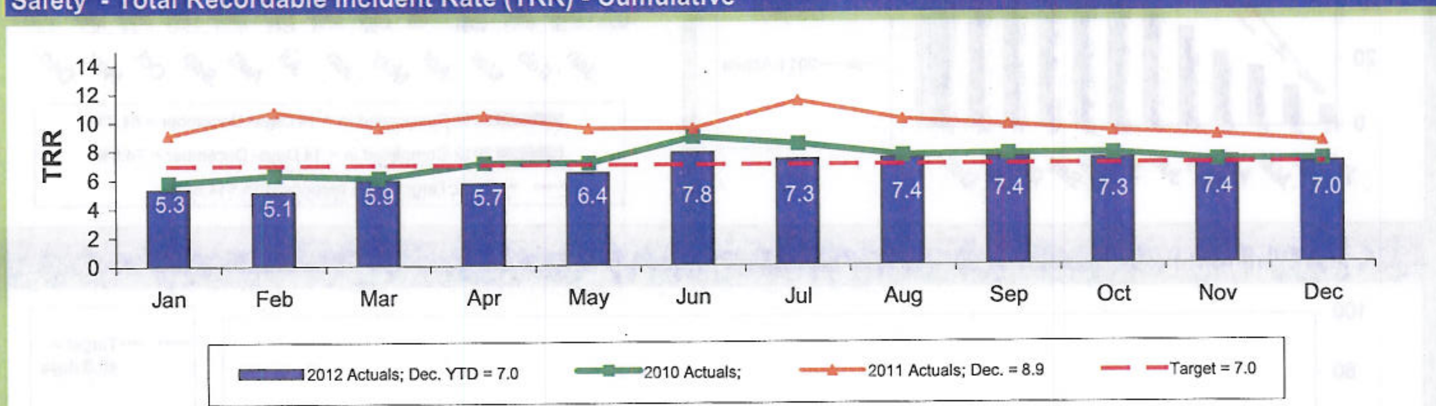


Vegetation Management - Cumulative Miles of Trees Trimmed



Human Resources:

Safety - Total Recordable Incident Rate (TRR) - Cumulative

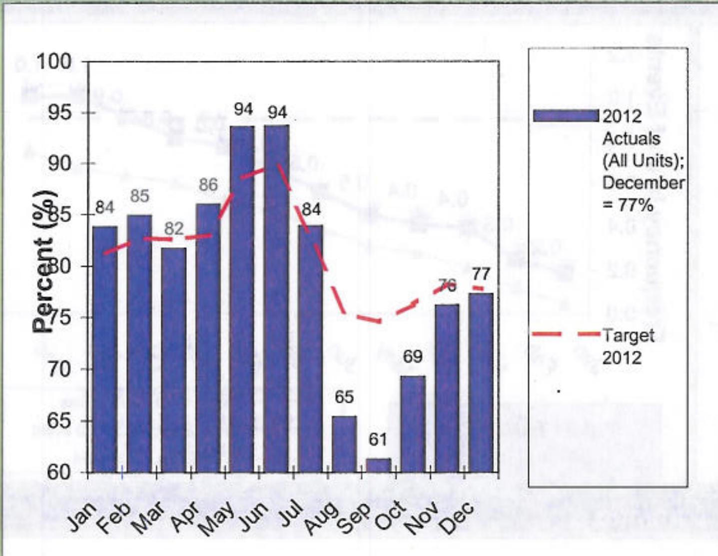


Hiring Statistics YTD

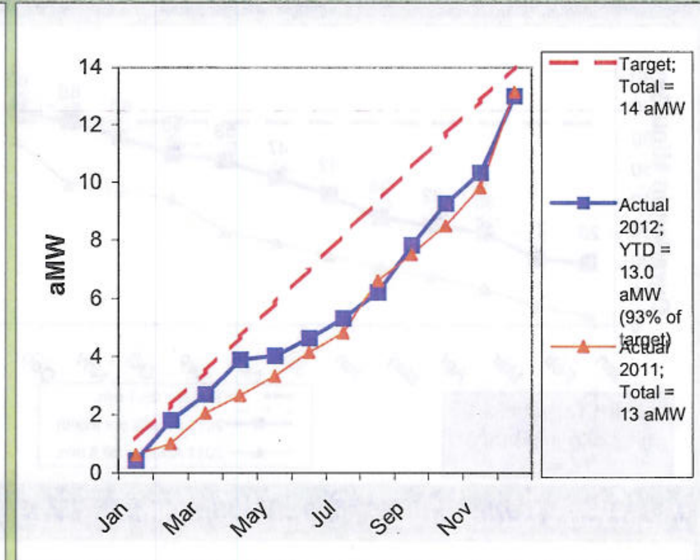
	Jan	Feb	Mar	April	May	Jun	Jul	Aug	Sept	Oct	Nov	Dec
Cumulative # of New Hires	8	27	37	44	55	60	67	72	84	96	104	122
Cumulative # of Promotions	5	12	12	18	20	21	22	27	36	42	47	49
Ave. # of Hiring Days	47	47	46	48	52	52	54	54	55	54	53	49
Cumulative # of Attrition	8	15	24	33	41	49	60	73	79	88	97	108
Vacancy Rate Mo. End	7.8%	7.3%	7.4%	7.3%	7.0%	7.3%	7.4%	7.6%	7.3%	7.3%	7.4%	7.0%

Power Resources:

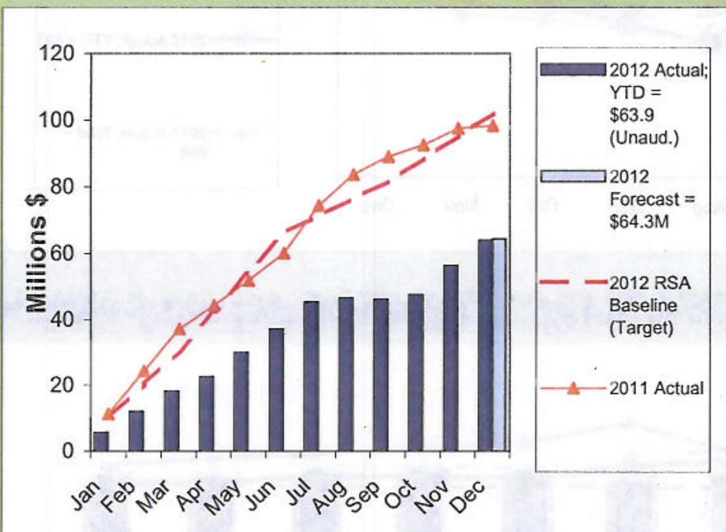
Generator Availability-All Units (Actuals %)



Conservation Savings (Cumulative)

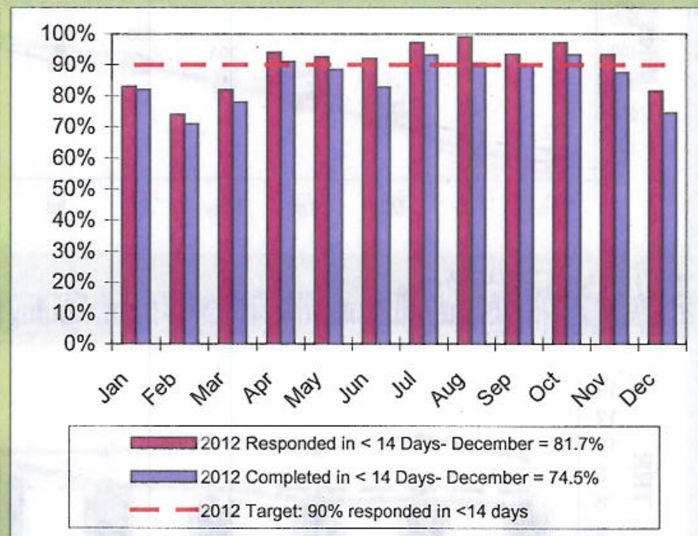


Net Wholesale Power Sales (Cumulative)



Customer Care:

Streetlight Repairs



Service Connections