

Seattle City Light Review Panel
c/o K. Kinney Seattle City Light
P.O. Box 34023 Seattle WA 98124-4023
CLRPquestions@seattle.gov

April 30, 2012

Honorable Mayor McGinn
The City of Seattle
600 Fourth Avenue
PO Box 94749
Seattle, WA 98124-4749

Dear Mayor McGinn:

As members of the City Light Review Panel, we are pleased to convey to you our endorsement of the Preferred Path in the Seattle City Light 2013-2018 Strategic Plan, as presented in the February 2012 public outreach draft document. We refer below to this draft document as the “Strategic Plan,” understanding that you are now considering what to transmit to the City Council for its action. We believe that of the five paths presented in the Utility’s Strategic Plan, the Preferred Path is the most appropriate alternative for City Light to pursue over the next six years.

The Strategic Planning Process

As previously conveyed in our letter of February 16, 2012, we are very pleased with the process that has been used to develop the Utility’s Strategic Plan, and Panel’s advisory role in that process. The effort has been time-intensive and thorough. We have met 32 times as a Panel over the course of two years, discussing and advising the Utility’s senior leadership with respect to the Strategic Plan. The Utility has been highly responsive to our questions and suggestions, and there has been a high level of engagement by the Panel members throughout the effort. The process has had good integrity and transparency. In addition, the process has included two extensive rounds of public input, through which we heard from hundreds of the Utility’s customers.

Rates: The “Baseline” Analysis and the Preferred Path

The Strategic Planning process incorporates two foundational analyses: (1) an assessment of City Light’s strengths, weaknesses, opportunities and challenges; and (2) a “Baseline” analysis of the costs to maintain the current level of service and reliability, including meeting mandates and completing projects and efficiency efforts already underway. The Baseline projects that an average annual rate increase of 4.1% per year over each of the next six years will be necessary. We believe the Baseline analysis reflects a credible, thorough assessment of the likely costs the Utility will incur to maintain current service levels, address mandates and complete ongoing projects and efficiency efforts. The Baseline is built on a series of assumptions: we find these assumptions to be reasonable but note they could change over the planning period (2013-2018).

The Preferred Path prescribes a series of investments, efficiencies and actions that are additive to the Baseline, and which will in total result in an annual average electricity rate increase estimated at 4.7% per year in each of the next six years. While any rate increase is challenging for residents and businesses

alike, in our view the most prudent path is to maintain current service levels and undertake the additional key investments and efficiencies outlined in the Preferred Path. Among the key investments are:

- a new substation in the north downtown area and an automated metering investment --both of which support overall system reliability;
- investment in workforce safety and in the Utility's ability to attract, train and retain a high quality workforce – both are critical in terms of basic operations and to address an impending wave of retirements (half the Utility's workforce is eligible to retire in the next five years);
- programs and tools that will improve effectiveness and efficiency – many investments targeting outdated, legacy technologies; and
- continued leadership in environmental stewardship.

Additional comments regarding some specific investment proposals are provided below, including the importance of rate predictability and avoiding rate spikes. In terms of the rate impact of the Preferred Path, we note that the industrial sector representative on the Panel, Matt Lyons, while supporting many aspects of the Strategic Plan, believes that increasing rates 31 percent over the next six years as called for in the Preferred Path will hit all rate payers, and particularly manufacturing and industrial businesses, very hard and he therefore does not support those proposed rate increases.

Driving Towards More Efficiencies: The Importance of Continued Benchmarking and City Support for More Flexibility in Labor Policies

We strongly endorse the importance of continuing to benchmark the performance of City Light against its national peers-- and to take steps to achieve parity with its peers in efficiency of operations and quality of service delivery. City Light is the 10th largest public utility in the nation. It operates in a national market—in terms of purchasing power (including renewable energy), and in terms of competing to attract and retain highly skilled staff. In other words, the Utility has a national peer group against which to benchmark itself. It is also important to track performance against internally-set performance targets. We are in agreement that City Light:

- Is making a solid effort in the area of securing efficiencies and has proposed to do what it reasonably can in this area over the Planning Period; and
- Should continue to examine and identify the drivers that are causing its performance and efficiency in some areas to be below its peer group average.

The City and the Utility should be commended for commissioning the national firm of UMS to develop a benchmarking study for City Light in 2011—and for developing a specific plan to follow up on the recommendations in that report. The Utility has identified 19 projects it plans to pursue in order to generate operating efficiencies that will reduce Baseline costs by \$18million within three years. These projects were selected based on general direction provided by the UMS Report. The Panel encourages City Light to be as transparent as possible about how the \$18M in savings will be achieved. The Panel intends to track the Utility's success in implementing the proposed efficiencies. The Utility indicates that of these 19 efficiency projects, seven will require changes in existing labor contracts and/or personnel rules. It is important that the Mayor and City Council support the Utility's need for flexibility in new

labor contracts and personnel system rules in order to be able to implement greater levels of operational efficiency. The Panel supports continued benchmarking in the future.

Endorsement of Key Strategic Plan Objectives: The Strategic Plan outlines four key strategic objectives, which the Panel endorses as the appropriate foundational pillars for the planning period:

1. Improve customer experience and rate predictability
2. Increase workforce performance and safety practices
3. Enhance organizational performance
4. Continue conservation and environmental stewardship leadership.

We offer comments below organized, as in the Strategic Plan, around these four key objectives.

Objective 1: Improve Customer Experience and Rate Predictability

We support the major investment in the North Downtown Substation that is included in the Preferred Path: this project supports system-wide reliability. We heard strong support during the Strategic Plan outreach as to the importance of reliable electric power.

We also strongly support the goal of rate predictability and changes to Net Wholesale Revenue calculation. When rates need to increase, this should be implemented on as steady a basis as possible, with significant advance notice wherever possible. Establishing the Rate Stabilization Account was an important first step in this regard. Adopting a six-year strategic Plan is the next step. And, we are persuaded that it is now time to re-examine the methodology for setting the Net Wholesale Revenue assumptions that go into building the Utility's budget. The more accurate these assumptions are, the more accurate the budget will be and the smoother rates will be. It does appear to us that more conservative assumptions around supply and market price assumptions about wholesale revenue are warranted.

We support actions that minimize the need for rate surcharges. The Panel supports taking actions to reduce the likelihood of rate surcharges—including temporarily lengthening debt term, undertaking additional refinancing, and assessing the timing of major projects-- while maintaining the Utility's bond rating. We feel such steps are appropriate in light of the current economic and financial environment. The Panel would like to revisit this issue over time to see if there are other ways to achieve this policy goal. Again, it is important to acknowledge that any rate increases are challenging for residents and businesses alike, and avoiding rate volatility is a critical part of addressing this issue for the Utility's customers.

The Panel is generally comfortable with pursuing the Advanced Metering Infrastructure (AMI) investment in 2015 , or later if necessary, to ensure that the Customer Information System (CIS) and Meter Data Management Systems are first solidly in place to support the AMI technology. The Utility needs to carefully design the rollout for AMI: outreach and education needs to be very well executed in order to address concerns that have surfaced in other communities. The Panel will seek to closely track this project as it proceeds, and has requested the Utility report to us at key milestone points.

It should be noted that the customer meters now in place are not digital, and are no longer manufactured. They will all have to be replaced, most sooner than later. In this sense, there is not a lot of choice in pursuing as least that aspect of the AMI project. Based on information provided to us, the trend nationally is towards implementing these systems, and City Light is lagging in pursuing this project. In sum, at some point in the future, the Utility will need this capacity, which serves as the foundation for future smart grid investments.

Objective 2: Increase Workforce Performance and Safety Practices.

Taking steps to improve workforce safety is a very important action item, for employees and the community. The Preferred Path includes a relatively small financial investment in workforce safety, but it is an investment we believe is absolutely necessary. As noted in the Strategic Plan, City's Light's reported injury record is *nearly twice the national average*. This is a serious issue that the Panel believes must be addressed.

The Utility should be allowed to implement policies and practices that enable it to better compete in the national market for needed staff expertise and to meet the objectives of the Strategic Plan. The Utility has mapped out an important initiative with respect to attracting and retaining a qualified workforce—at all levels of the organization. We endorse this effort and we further recommend the City should, as requested by the Utility, adopt a compensation philosophy that allows City Light to better attract professional staff. This means providing City Light with flexibility to develop compensation and classification requirements to meet its needs. As noted, the Utility operates in a national market, competing with other utilities regionally and nationally to attract and retain highly skilled staff. We are told that nearly a third of the City Light leadership and subject matter expert positions are paid between 10-40% less than their industry peers, without taking into account cost-of-living differentials which make the pay gap even greater. In addition, over half the utility's workforce will be eligible to retire in the next five years. City Light's employee age profile is common to utilities across the country. Without a competitive compensation, training and retention program, City Light will be ill-equipped to meet the impending wave of retirements and attract the necessary personnel. Additionally, we recommend the Utility be more involved in discussions with labor partners, to help insure the Utility can meet the objectives of the Strategic Plan. The Utility must address these human resource challenges in order to position itself for success.

Objective 3: Enhance Organizational Performance.

Benchmarking and efficiencies are central to this effort and have been discussed above. The Panel acknowledges and supports the importance of the other initiatives within the Preferred Path that will improve organizational performance. Many of these are technology and systems upgrades—ranging from completing the Utility's "IT Roadmap," to undertaking a comprehensive performance-based reporting effort, to project management quality improvement, to entering into internal service agreements with City central service departments. To become a high performing organization, the Utility must be given an opportunity to improve the tools available to it, and be encouraged to focus on delivering the most efficient, effective service possible.

Objective 4: Continue Conservation and Environmental Stewardship Leadership.

The Utility is carbon neutral and has an aggressive conservation and energy efficiency program in place. By endorsing the Preferred Path, we are acknowledging the value of the aggressive energy efficiency program included in the Baseline. The Utility's Integrated Resource Plan supports these efficiency acquisitions as the most prudent approach to meeting the Utility's future power needs and mitigating risk from uncertainty in water resources. This approach makes good business sense and should be continued.

Consideration of Other Alternatives in the Strategic Plan

We are supporting the Preferred Path in lieu of Alternate Paths 4 (More Aggressive Reliability Investments) and 5 (Bolder Environmental Initiatives). While both Alternative Paths include some worthy proposals, we believe the highest priority items are those included in the Preferred Path. The Utility will have a very full plate to be able to successfully move ahead on these items, and our endorsement of the Preferred Path reflects our desire that the City and the Utility focus on accomplishing the Preferred Path in the next six years.

The Panel's Work Ahead

For the remainder of 2012, the Panel will focus on rate design and cost allocation. We also will work with the Utility to develop means through which we can track the Utility's progress in implementing the Strategic Plan. Also, while we hope that our own efforts provide an important new level of oversight to the Utility, we will consider whether there are other governance-related matters that should be part of City Light's strategic planning framework.

Acknowledgements

We thank Superintendent Carrasco and the Utility's executive team for their many hours of dedicated effort and leadership in the strategic planning effort. We also thank the City Councilmembers, their staff, and the Mayor's Office for their participation and input throughout the process.

In closing, we believe that implementing the Preferred Path will place City Light in a much stronger position to serve its customers in the years ahead and will improve the efficiency of City Light's operations. We cannot overstate the importance of a longer-term approach to oversight of the Utility. Adopting a six-year strategic plan, and providing oversight and support of the Utility's work over that time to achieve specific objectives within prescribed rate limits will be a major step forward for the

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Honorable Mayor McGinn

April 30, 2012

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Utility and its customers. We encourage your support for the Preferred Path.

Sincerely,

City Light Review Panel



Stan Price, Co-Chair

Panel Position 3:
Non-Profit Energy
Efficiency Advocate



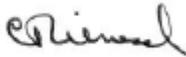
Eugene Wasserman, Co-Chair

Panel Position 8:
At-Large Customer



David Allen

Panel Position 5:
Commercial Customer



Tom Lienesch

Panel Position 1:
Economist



Matt Lyons

Panel Position 6:
Industrial Customer



Julia M. Ryan

Panel Position 2:
Financial Analyst



Sue Selman

Panel Position 7:
Low-Income Customer
Representative



Debbie Tarry

Panel Position 9:
Suburban Franchise Customer

(Position 4 Currently Vacant)

cc: Seattle City Councilmembers
Jorge Carrasco, Superintendent, Seattle City Light