Seattle City Light

MEMORANDUM

FEBRUARY 23, 2015

TO
Ed Murray, Mayor
Seattle City Council

FROM
Jorge Carrasco, General Manager and CEO

SUBJECT
Financial Update – December 2014 (PRELIMINARY)

This memo provides an analysis of Seattle City Light's financial condition and operating results through December 31, 2014. The attached Income Statement Analysis, which is summarized in the table below, provides a summary of how City Light performed in 2014 compared to the same period the previous year and the 2014 Financial Plan. The 2014 Financial Plan is based on the revenue and expense projections included in the adopted budget for 2014.

FINANCIAL HIGHLIGHTS
December 31, 2014

$ in millions	Year End Dec. 31 2014	2013	Plan	Actual vs. Plan
Retail Power Revenues[1]	$ 728.4	$ 697.7	$ 754.0	$ (25.6)
Net Wholesale Energy Sales[2]	$ 88.6	$ 51.5	$ 85.0	$ 3.6
Net Power O&M	$ (253.9)	$ (245.5)	$ (265.0)	$ 11.1
Net Non-Power O&M	$ (211.1)	$ (209.2)	$ (222.5)	$ 11.4
RSA Transfers, Net[3]	$ (4.4)	$ 18.3	$ (2.7)	$ (1.7)
Taxes, Depreciation & Other	$ (219.6)	$ (200.1)	$ (228.8)	$ 9.2
Net Income	**$ 128.0**	**$ 112.7**	**$ 120.0**	**$ 8.0**
Operating Cash	$ 128.3	$ 193.8	$ 248.5	$ (120.2)
Construction Account - Restricted	$ 123.8	$ 58.5	$ -	$ 123.8
Rate Stabilization Account	$ 114.4	$ 110.0	$ 112.6	$ 1.8
Bond Reserve	$ 47.9	$ 46.8	$ 69.8	$ (21.9)
Other Restricted Assets	$ 12.3	$ 11.7	$ 11.9	$ 0.4
Total Cash	**$ 426.7**	**$ 420.8**	**$ 442.9**	**$ (16.2)**
Debt Coverage Ratio	1.86	1.85	1.88	(0.02)
Debt to Capitalization Ratio	59.8%	61.8%	60.9%	-1.2%

(1) Retail power revenues include revenues such as Green Power Program and power factor charges.

(2) Revenue from wholesale sales, before booked out long term purchases.

(3) Transfers from the RSA less transfers to the RSA.

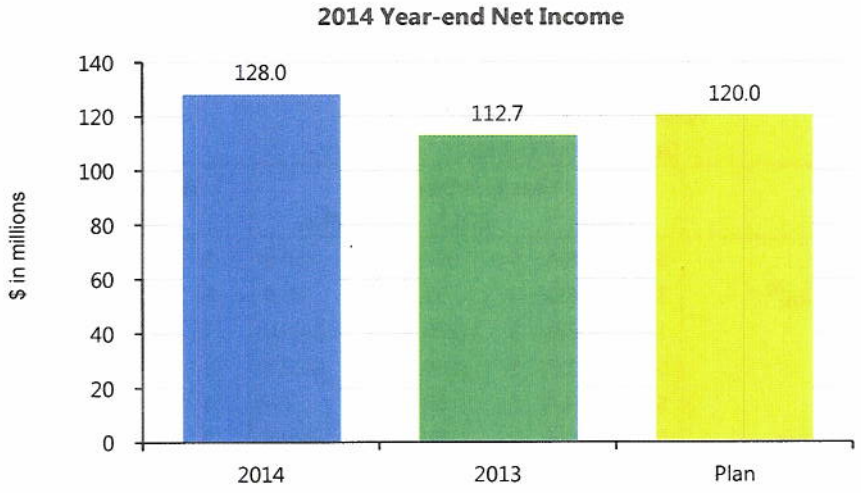
YEAR-END NET INCOME, RELATIVE TO 2013

As indicated in the table and charts on the previous page, net income for the period ending December 31, 2014 was $128.0 million, which is $15.3 million or 13.6% favorable compared to the same time period in 2013. The increase was due primarily to the following factors:

- A $30.7 million increase in retail power revenues primarily driven by the $.009/kWh BPA pass-through effective October 1, 2013 as well as the 5.6% system average rate increase effective January 1, 2014.
- A $22.7 million decrease in net transfers to the rate stabilization account. In 2013, due to a number of operational savings, $21.0 million in cash from the Light Fund was transferred to the rate stabilization account in order to delay an anticipated surcharge in early 2014.
- A $20.3 million reduction in capital contributions driven by two significant in-kind CIAC contributions (Mercer Street and Amazon) received in September 2013.

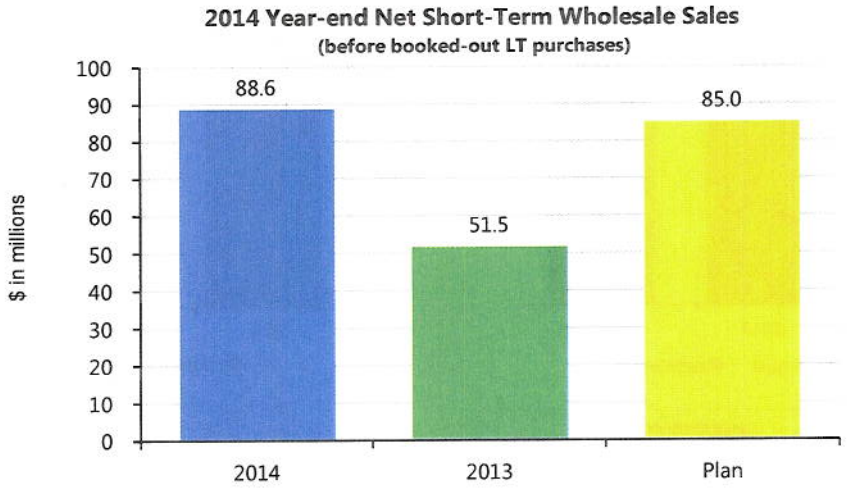
YEAR-END NET INCOME, RELATIVE TO PLAN

Net income for 2014 is $128.0 million, which is $8.0 million or 6.7% favorable to Plan. The difference is driven primarily by higher power revenues combined with lower net non-power O&M, interest, and long-term purchased power costs. These favorable variances were partially offset by lower retail revenues and lower in-kind capital contributions.

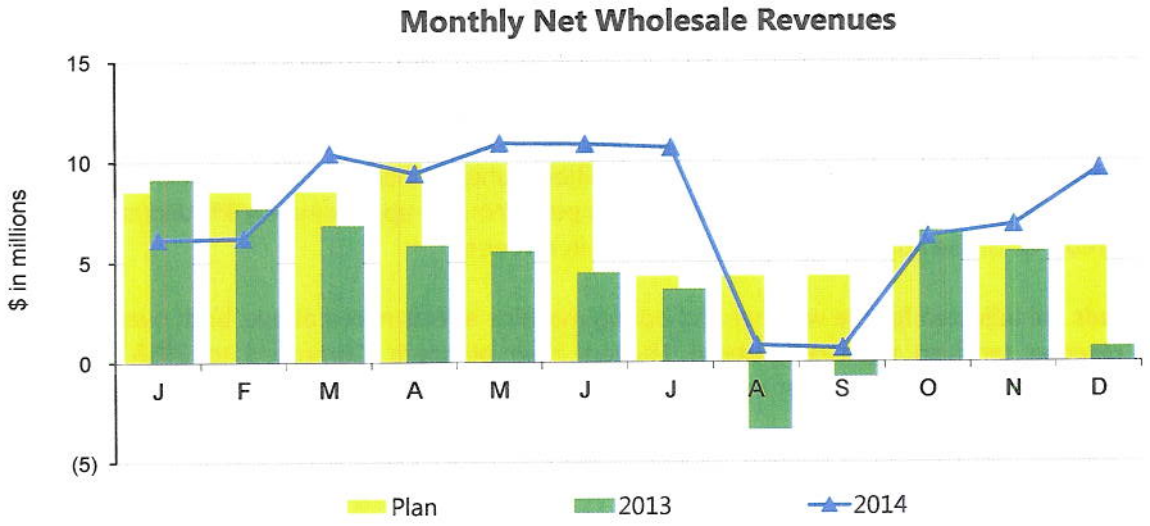


NET SHORT-TERM WHOLESALE ENERGY

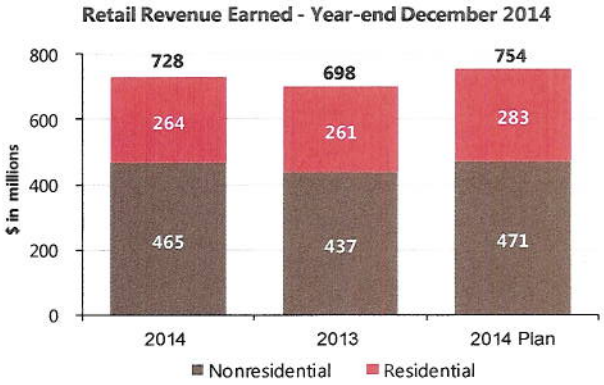
December year-end net wholesale revenues of $88.6 million increased $37.1 million or 72% from 2013 driven by a combination of higher volume and higher average sales price. Compared to the baseline of $85.0 million, full-year revenues were favorable by $3.6 million or 4.2%.



December 2014 net wholesale revenues were $9.6 million, up $8.9 million from the prior year due to exceptionally low hydro flows in December 2013.



RETAIL POWER REVENUES



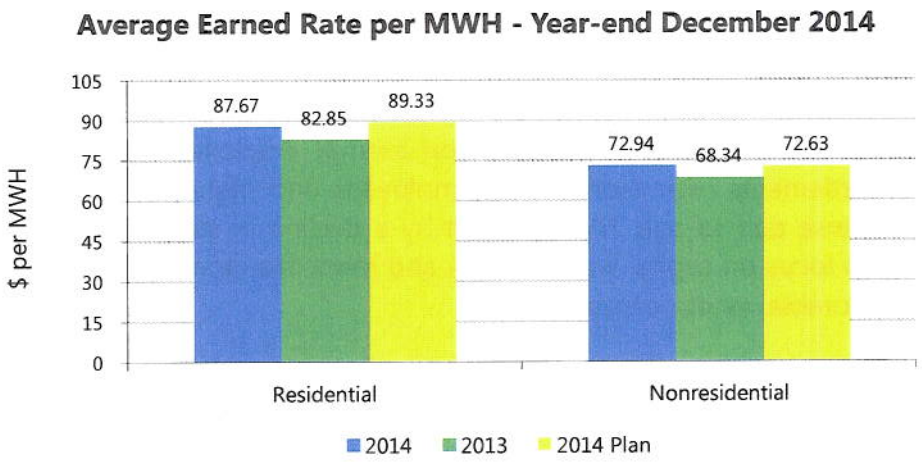
	Retail MWh YTD		
	Nonresidential	Residential	Total
2014 vs 2013	0.1%	-3.9%	-1.2%
2014 vs Plan	-1.8%	-5.0%	-2.8%

	Retail Revenue YTD		
	Nonresidential	Residential	Total
2014 vs 2013	6.3%	1.1%	4.4%
2014 vs Plan	-1.4%	-6.8%	-3.4%

2014 load was lower than planned by about 274 GWh, or 2.8%. About half of the residential shortfall was accounted for by warmer than normal weather (less heating load). The nonresidential difference was due entirely to the decreased load of the Alaskan Way tunnel boring machine. The latter result means that other 2014 nonresidential load (mostly business load) was right on target compared to the 2014 plan.

While 2014 revenue was 4.4% higher than the amount received in 2013, it was also 3.4% lower than planned because of the same two effects noted above and the additional unexplained reduction in residential load. While there were slight differences in expected vs actual revenue per MWh, the approximately 3% decrease in load accounts for almost all of the approximately 3% reduction in revenue.

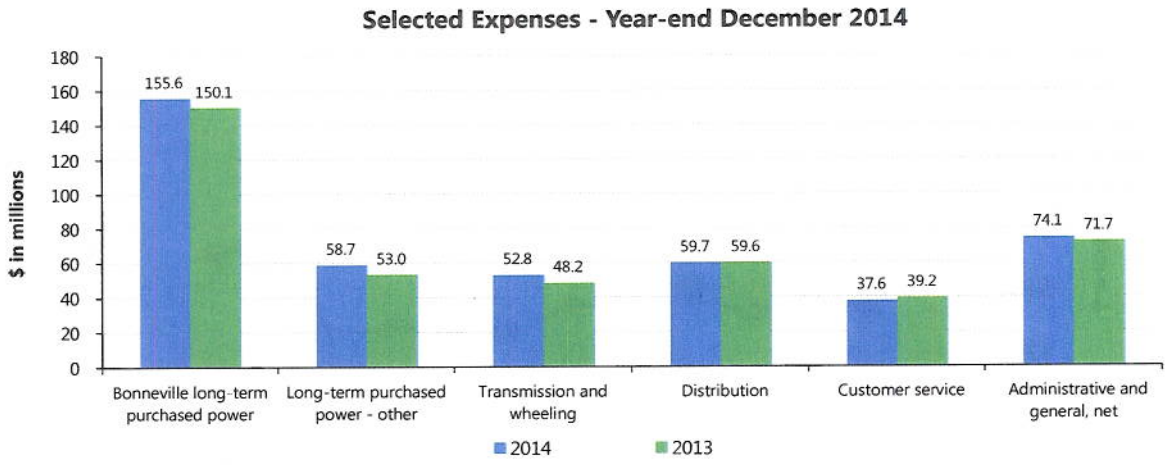
When 2014 loads are adjusted for the weather and boring machine effects noted above, both overall consumption and overall revenue received were only about 1% less than planned. Compared to 2013, with the same adjustments, 2014 consumption was lower by 0.2% and 2014 revenue was higher by 5.6%.



The actual average earned rate per MWh for residential and nonresidential customers is different from what was expected in the 2014 Plan due to slight differences in assumed versus actual patterns of consumption.

DATA FOR SELECTED ACCOUNTS

The following chart presents full-year 2014 data for major components of City Light's operating expenses excluding wholesale power transactions. These expenses can fluctuate month to month compared to the previous year for a number of reasons including work scheduling and accounting adjustments. Major or noteworthy differences from 2013 are detailed below.



- Bonneville expenses: Higher due to higher BPA power charges effective October 2013 and an increased block load shaping rate which are partially offset by a larger slice true up credit recorded in January.

- Long-term purchased power: Higher due to increased prices and volume for purchases, fair value recording of energy exchanges and lower booked out long term purchases.

- Transmission and wheeling expenses: Higher due to higher BPA wheeling charges as a result of higher transmission rates.

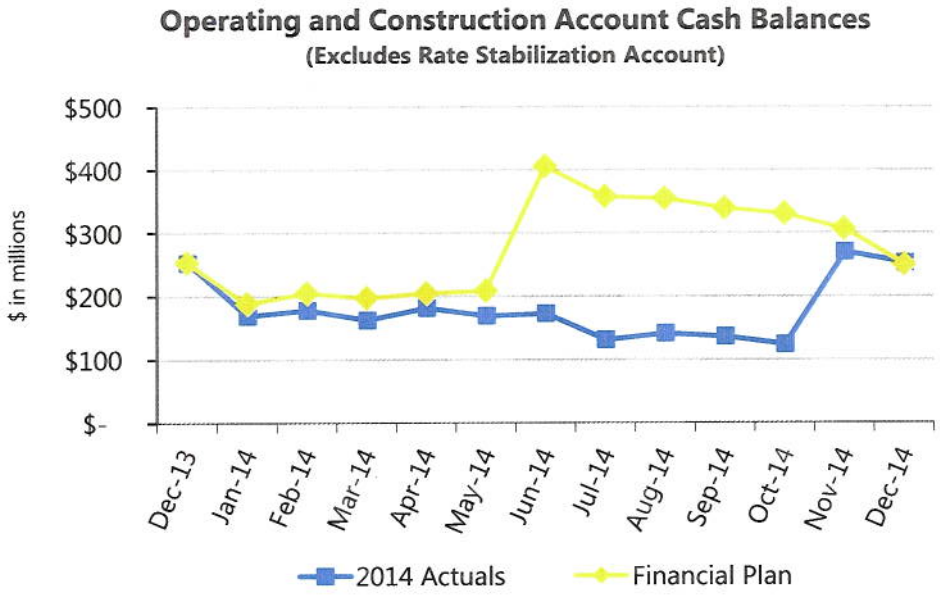
- Distribution costs: Higher due to retroactive non-exempt employee pay going back to 2013 resulting from settlements with represented employees and higher underground equipment maintenance expense due to age. Mostly offset by a decline in substation expenses resulting from an increased focus on capital work in 2014 and lower tree trimming expenses driven by a new and more favorable vendor contract.

- Customer service expenses: Lower due to a decrease in bad debt expense resulting from an improved estimation methodology that better reflects actual expense. This was partially offset by increased temporary staffing for both low-income outreach and meter reading as well as higher customer contract expenses due to increased service connections.

- Administrative and general expenses: Higher due to general office salary increases, a lower vacancy rate and higher attorney and other professional service fees.

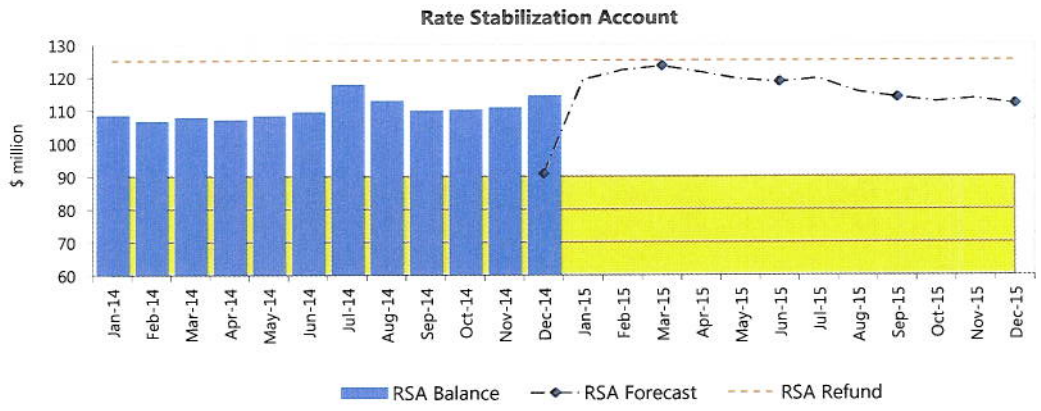
CASH POSITION

As of December 31, 2014, City Light's operating plus construction account cash balance was $252.1 million, just slightly higher than the amount in the 2014 Financial Plan of $248.5 million. The variances from the Financial Plan during the year were due to a postponement of the 2014 bond issue from June to October (with receipt of funds in November) and a smaller bond issue size.



RSA POSITION

The cash balance in the RSA was $114.4 million as of December 31, 2014. No surcharge is currently forecasted for 2015.



2014 BUDGET

As of December 2014, City Light is within its budget authority through year-end 2014. The Department has spent 95% of the overall O&M budget (O&M budget includes non-power O&M expenses, purchased power, taxes and debt service) through year-end 2014. City Light's spending on the Capital Program through December is 84% of the 2014 year-end forecast.

DEBT-TO-CAPITALIZATION

As of December 31, 2014, City Light's debt-to-capitalization ratio was 59.8%, which is lower than both the Plan ratio of 60.9% and the December 2013 ratio of 61.8%. The favorable variance from Plan was driven by a combination of a lower than planned debt issue and higher than planned net income. The favorable variance from 2013 was due primarily to a 13.6% increase in net income.

COMPLIANCE

Attached for your information is the City Light Risk Oversight Status Report as of January 21, 2015, 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 2014, with 2013 data included for comparison, is attached.

Attachments

Line No.	Condensed Statements of Revenues, Expenses and Changes in Net Position	Year-to-date		Year Ending December 31, 2014		
1		[A]	[B]	[A - B]	[D]	[A - D]
2	**Unaudited**	Actuals December 31, 2014	Actuals December 31, 2013	Actuals to Actuals Variance	2014 Financial Plan	Variance
3	In millions					
4	**Operating Revenues**					
5	Retail power revenues	$ 728.4	$ 697.7	$ 30.7	$ 754.0	$ (25.6)
6	Short-term wholesale power revenues, net (lines 40 + 43)	96.8	63.0	33.8	105.2	(8.4)
7	Power-related revenues - other	50.8	40.4	10.4	44.8	6.0
8	Transfers from/(to) rate stabilization account	(4.4)	18.3	(22.7)	(2.7)	(1.7)
9	Other revenues	22.4	22.8	(0.4)	24.3	(1.9)
10	Total operating revenues	894.0	842.2	51.8	925.6	(31.6)
11	**Operating Expenses**					
12	Generation	34.8	40.0	(5.2)	43.4	(8.6)
13	Bonneville long-term purchased power	155.6	150.1	5.5	155.7	(0.1)
14	Long-term purchased power - other	58.7	53.0	5.7	65.2	(6.5)
15	Short-term wholesale power purchases	14.9	19.8	(4.9)	25.2	(10.3)
16	Power-related wholesale purchases - other	17.7	14.1	3.6	17.5	0.2
17	Other power costs	13.2	12.2	1.0	11.5	1.7
18	Transmission and wheeling	52.8	48.2	4.6	55.0	(2.2)
19	Distribution	59.7	59.6	0.1	64.7	(5.0)
20	Customer service	37.6	39.2	(1.6)	42.1	(4.5)
21	Conservation	27.3	21.5	5.8	23.9	3.4
22	Administrative and general, net	74.1	71.7	2.4	72.7	1.4
23	Taxes	82.7	79.3	3.4	86.3	(3.6)
24	Depreciation and amortization	105.8	102.3	3.5	108.0	(2.2)
25	Total operating expenses	734.9	711.0	23.9	771.1	(36.2)
26						
27	**Net Operating Income**	**159.1**	**131.2**	**27.9**	**154.5**	**4.6**
28						
29	**Other Deductions, Net**					
30	Investment Income	7.9	0.8	7.1	6.5	1.4
31	Other income (expense), net	6.8	7.1	(0.3)	5.8	1.0
32	Interest expense	(77.9)	(79.3)	1.4	(85.8)	7.9
33	Noncapital grants	3.8	3.2	0.6	4.0	(0.2)
34	Capital contributions	27.6	47.9	(20.3)	34.1	(6.5)
35	Capital grants	0.7	1.8	(1.1)	1.0	(0.3)
36	Total other deductions, net	(31.1)	(18.5)	(12.6)	(34.5)	3.4
37						
38	***Change in Net Position***	**$ 128.0**	**$ 112.7**	**$ 15.3**	**$ 120.0**	**$ 8.0**
39	**Note A:**					
40	Short-term wholesale energy sales, gross	103.5	71.3	32.2	110.2	(6.7)
41	Short-term wholesale energy purchases	(14.9)	(19.8)	4.9	(25.2)	10.3
42	**Net ST wholesale sales before booked-out LT purchases**	**88.6**	**51.5**	**37.1**	**85.0**	**3.6**
43	Booked-out long term purchases	(6.7)	(8.3)	1.6	(5.0)	(1.7)
44	Net short-term wholesale energy sales	**81.9**	**43.2**	**38.7**	**80.0**	**1.9**
45	**Note B:**					
46	Power-related revenues, net (line 7 minus line 16)	33.1	26.3	6.8	27.4	(1.7)

Net Income Variance Analysis
December 2014

Variance Year-to-Date 2014 Compared to 2013 Actuals: $15.3 million or 13.6%

Major components ($ in millions):

$112.7	Net Income YTD through November 30, 2013
$30.7	Higher retail revenues due to 5.6% rate increase effective January 1, 2014 and 1.2% BPA pass-through rate increase effective October 1, 2013.
$37.1	Higher net wholesale energy sales
($22.7)	Lower transfers from RSA year-to-date due to higher net wholesale revenues
($5.5)	Higher BPA power due to fluctuations in block load quantities and rate
$5.2	Lower generation due primarily to write off of Gorge second tunnel plans in 2013
($5.7)	Higher long term energy purchases primarily from King County co-generation and Lucky Peak combined with lower book-out offsets. Transactions include both cash and fair value.
($4.6)	Higher BPA wheeling and transmission as a result of higher transmission rates in 2014
($2.4)	Higher administrative and general, net, due primarily to increases in salaries and hiring
$7.1	Higher investment income due to gains in fair market value of cash pool investments y-t-d
($3.4)	Higher taxes due to higher revenues
($5.8)	Higher conservation costs due to increased amortization resulting from 2014 additions to conservation assets
($20.3)	Lower in-kind CIAC primarily due to non-recurring Mercer Street and Amazon 2013 projects
$6.8	Higher other power-related revenues due primairly to Grant County exchange transactions beginning in July 2014
($1.2)	Other (net)
$128.0	Net Income YTD through December 31, 2014

Variance 2014 Actuals Compared to Financial Plan: $8.0 million or 6.7%

Major components ($ in millions):

$120.0	Net Income through December 31, 2014 - Financial Plan
($25.6)	Lower retail revenues than plan
$8.6	Lower generation
$6.5	Lower long term energy purchases
$5.0	Lower distribution
$4.5	Lower customer service
$3.6	Lower taxes
$3.6	Higher net wholesale energy sales
$5.7	Higher other power-related revenues
($6.5)	Lower capital contributions
$2.6	Other (net)
$128.0	Net Income YTD through December 31, 2014

Seattle City Light
Risk Oversight Status Report
As of January 21, 2015

Summary

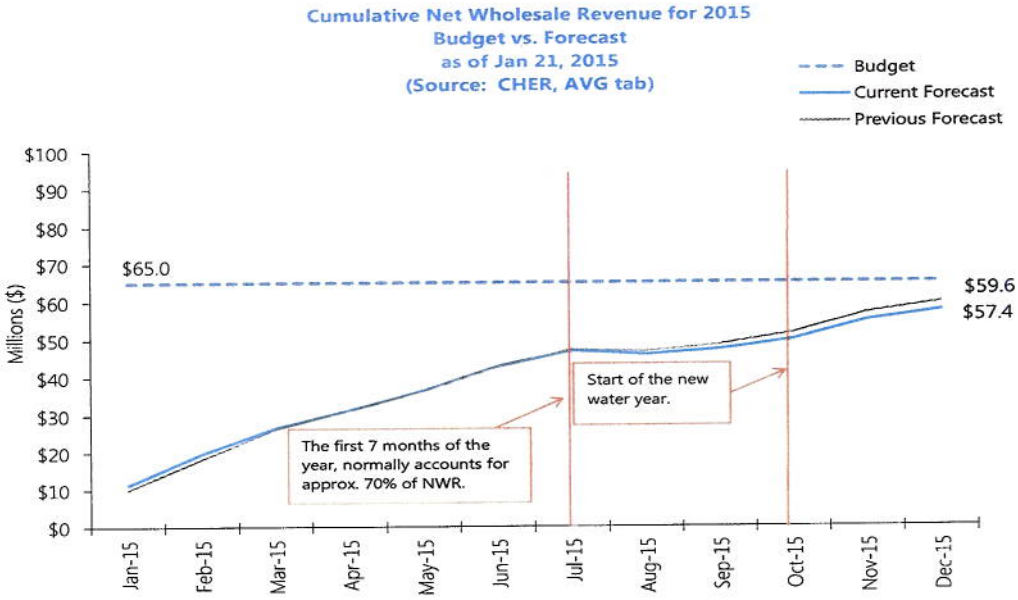
	5 Year Average	2015 Average	% of 5 Year Average
SCL Hydro Generation	1,099 MW	1,053 MW	96%
Market Prices (Peak Hours)	$32.67	$26.78	82%

SCL Hydro Generation: This shows the total average generation per hour for Seattle City Light's three major hydroelectric resources (Skagit, Boundary, and BPA Slice). For the 2015 calendar year this average includes actual generation for past months and forecasted MW for future months. The 5 year average value is comprised of actual generation for the years 2010-14. The percent of 5 year average shows the generation for the current year relative to the 5 year average.

Peak Market Prices: This shows the total average price per hour for peak hours at the nearest and the most active electricity trading hub (MID-C). For the 2015 calendar year this includes the average Dow Jones firm peak index daily prices for past months and the average of the monthly forward marks for the future months. The 5 year average is computed from the Dow Jones peak daily prices for the years 2010-14. The percent of 5 year average shows the market prices for the current year relative to the 5 year average.

Wholesale Revenue Variance: Chart 1 below compares the approved 2015 Net Wholesale Revenue (NWR) budget of $65MM with the latest NWR forecast of $57.4MM. The NWR forecast decreased by $2.2MM from the previous forecast of $59.6MM. This decrease in revenues resulted from decrease in resources from February to December -- accounting for approximately $3.9MM. This decline was partially offset by increase in revenues by $1.3MM and $0.4MM resulting from increase in January estimates and power prices respectively.

Chart 1



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 Marketing Division (PMD) must conduct its hedging activity to maintain the Utility's position within established Risk Tolerance Band (RTB) of $8MM based on the calculated 5% Tail Risk metric. For the prompt year (the year immediately following the current calendar year), the established RTB is $10MM.
(Section 3.3.2 Prompt and Within the Month (WERM))

Prompt Month & Within Month Volumetric Limit: The Power Marketing Division (PMD) 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 physical 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 Marketing Division (PMD) will immediately suspend any further forward sales for the future calendar quarter, within the next 24 months period, if the forecasted net combined system energy projected surplus for that quarter is less than zero, at 25th percentile. Further, the PMD will take immediate action to purchase if the forecasted net combined system energy position for a future calendar quarter, in the next full 24 months period, is less than zero at 50th percentile. Such corrective action shall reduce the said deficit to zero at 50th percentile for that quarter.
(Section 3.3.1.2 Forward Month's Resource Requirement (WERM))

Forward Sales Limit: The Power Marketing Division (PMD) will not sell forward a quantity of more than 1,750,000 net megawatt hours over a rolling four full calendar quarters. Such limit will be calculated as the net position of City Light's combined physical position adjusted for any physical 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 Marketing Division (PMD) 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 $2MM for option premiums for any calendar year.
(Section 3.3.1.4 Forward Month's Resource Requirement (WERM))

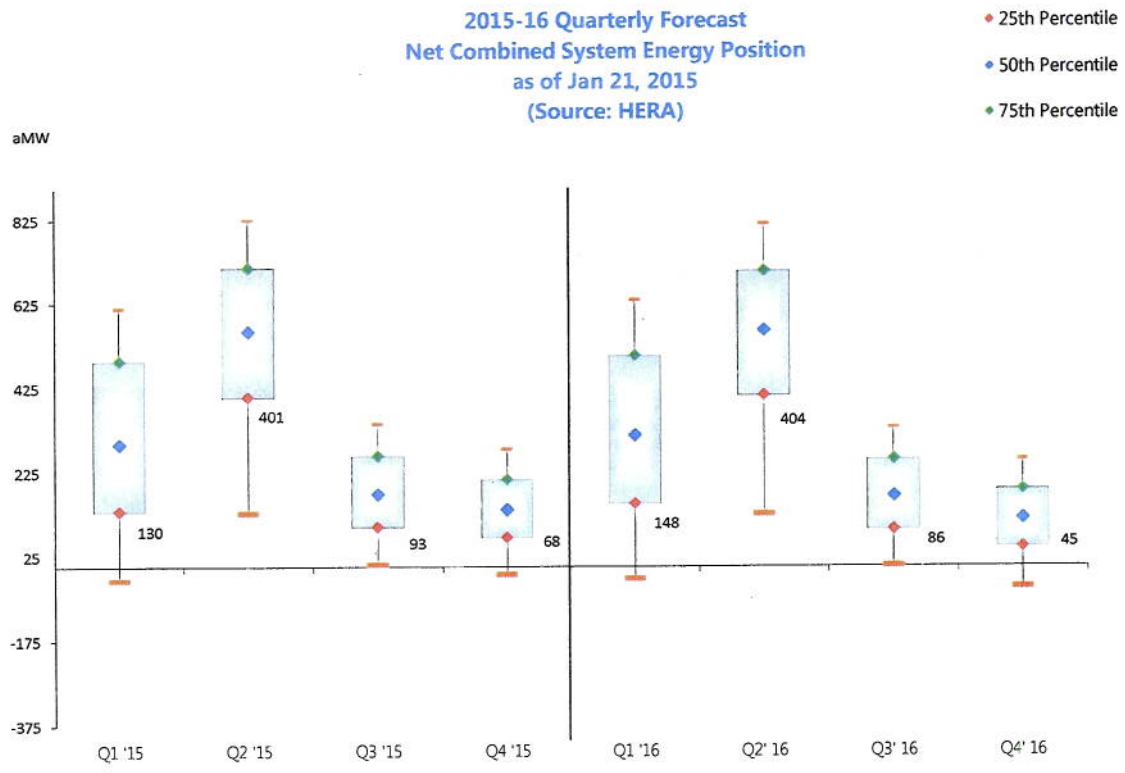
Hedging Plan & Position Status

Hedge Plan 2015, Phase 1 was last proposed and approved by the Risk Oversight Council on Dec 23, 2014.

City Light uses the most recent load and hydro forecasts including relevant historical data to run a Historical simulation based model that produces a forecast of more than two thousand portfolio resource scenarios. The output of this model along with the current forward positions provides energy information needed to determine SCL's position. Shown below in Chart 2 are positions as of the model run date for the different resource scenarios.

Chart 2 shows the Net Combined System Energy Position for the next quarters to match City Light's short-term transacting authority. The blue boxes represent the expected net energy position from 25th to 75th percentile. The dark blue diamonds inside the boxes represent the 50th percentile. If the blue diamond falls below zero, City Light must purchase adequate energy to cover that deficit.

Chart 2



5% Tail Risk Metric, 2015

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.

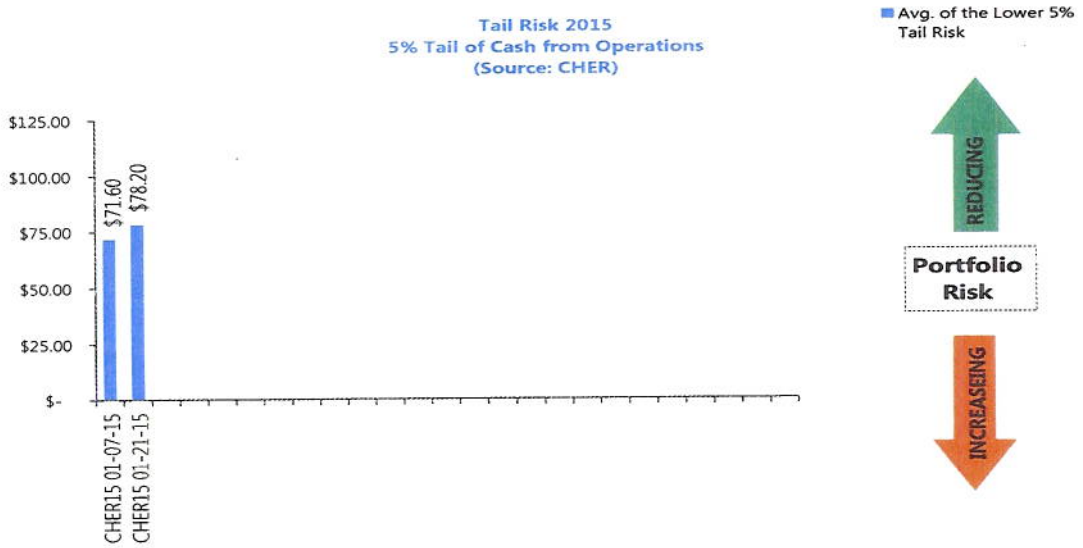
In 2011, the Rate Stabilization Account (RSA) became operational. The RSA is a cash reserve that is used to buffer the Utility from uncertainty in wholesale energy revenue. If the RSA becomes depleted, it is replenished via retail rate surcharges. The RSA significantly mitigates City Light's financial (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). This metric shows the utility's portfolio position as of that week.

Chart 3 (below) illustrates the 5% Tail Risk metric values for the calendar year 2015. The current projection of a worse case of Cash from Operations is $78.20 MM.

Chart 3



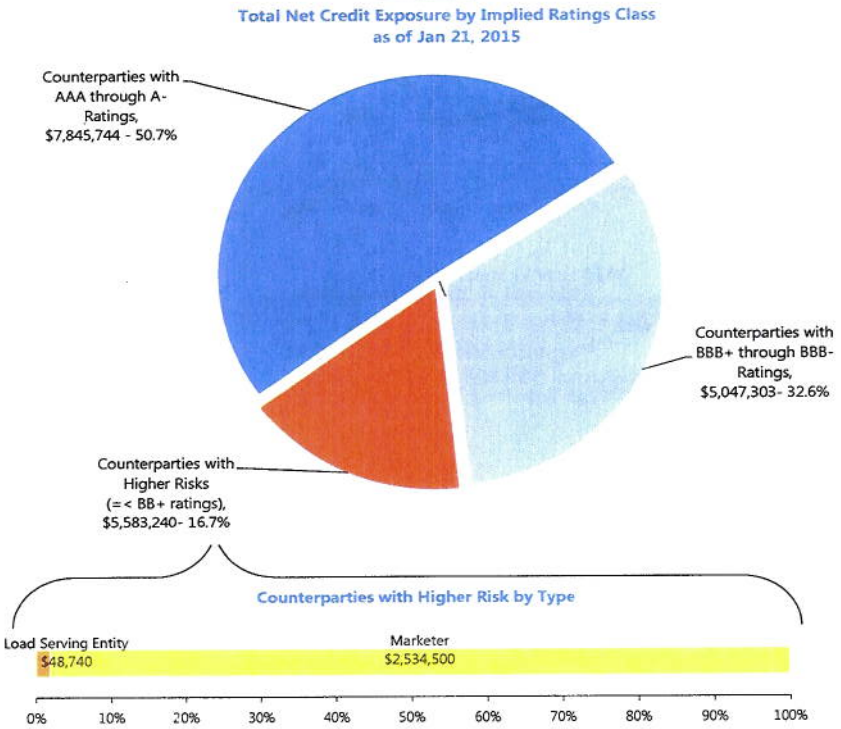
Credit

City Light actively manages its wholesale counterparty credit risk by:

I. setting credit limits for each counterparty that are derived from a credit limit framework, credit scoring model and analysis;
II. securing credit enhancements when necessary;
III. monitoring national and global news including news related to industry and specific to counterparties;
IV. daily monitoring of counterparty credit exposures.

Risk Management Division uses industry standard tools to proactively measure changes in counterparty creditworthiness. Implied credit ratings are utilized in conjunction with standard ratings provided by external agencies. The concept of risk tolerance extends to counterparties that are considered 'Higher Risk' with equivalent Moody's and S&P implied ratings of 'BB+' or less. Counterparties with such implied ratings are placed into the 'Higher Risk Credit Portfolio' for close monitoring in order to reduce the risk of delayed or non-payment while utilizing wholesale power, transmissions and related ancillary revenue opportunities. City Light strives to keep its "Higher Risk" counterparty exposures at less than 25% of the total exposure at any given time. However, this percentage can vary based on the time of the month when the report is produced.

Chart 4

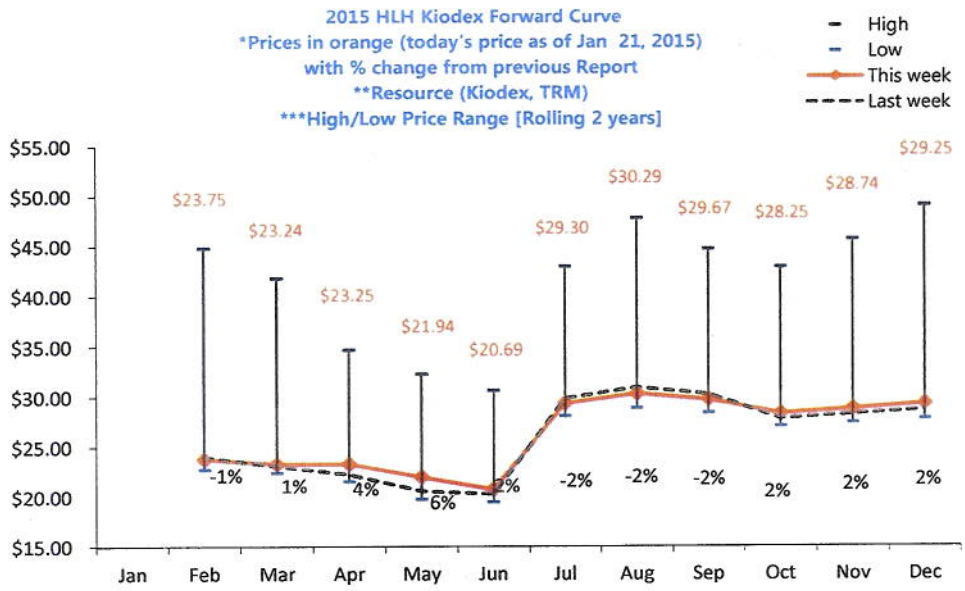


Credit Notes: Risk Oversight is negotiating a new parent guaranty with an existing counterparty. A parent guaranty was in place for the counterparty, but it elected to terminate the guaranty two months ago as trade activity declined. However, the counterparty has now changed its position and is seeking increased trading with SCL.

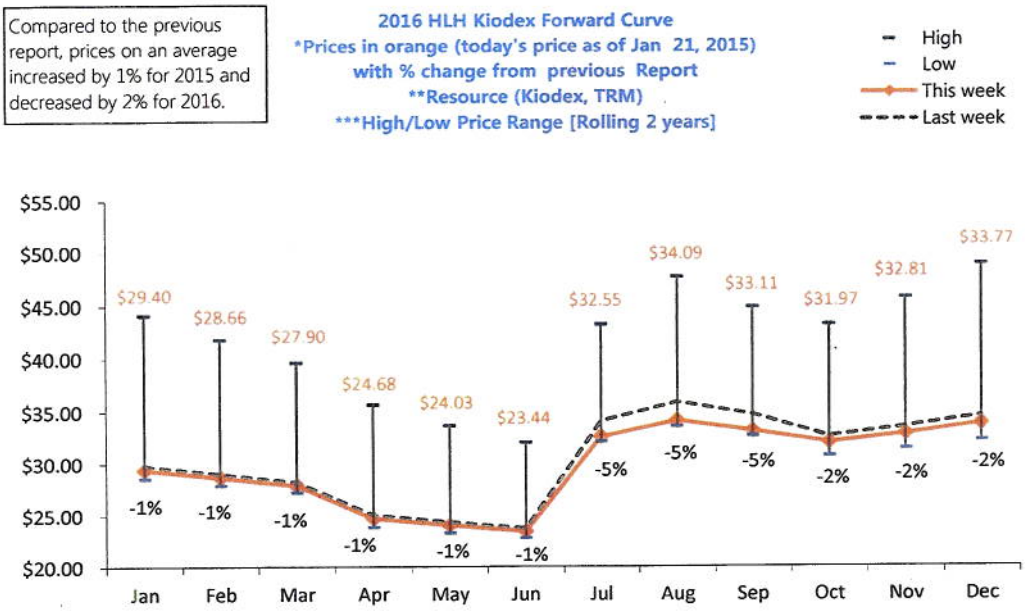
Price

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 2015 & 2016.

Chart 5



Compared to the previous report, prices on an average increased by 1% for 2015 and decreased by 2% for 2016.



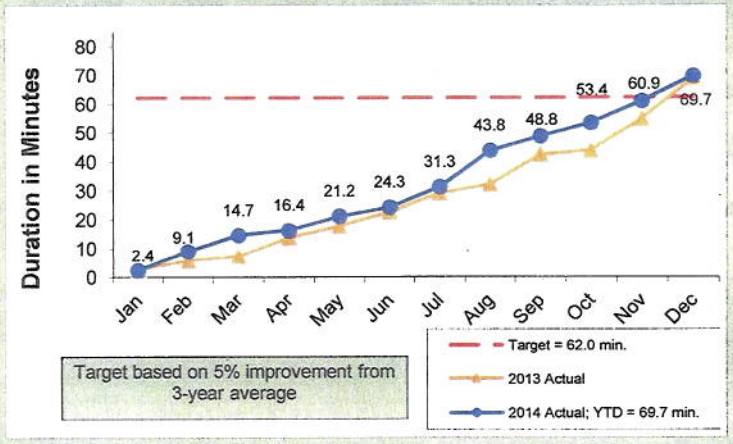
Seattle City Light

Performance Metrics Report

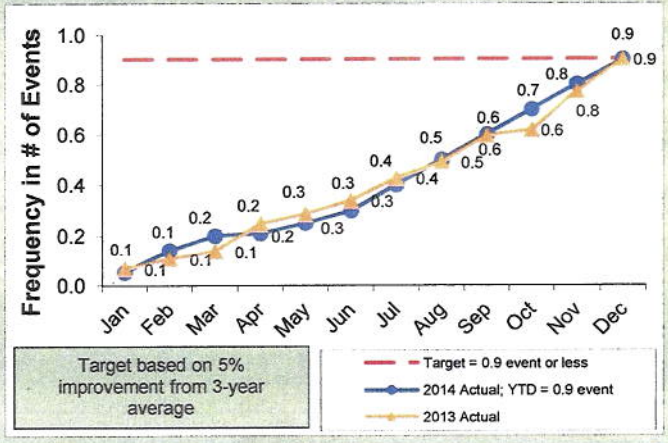
December 2014

Distribution Operations:

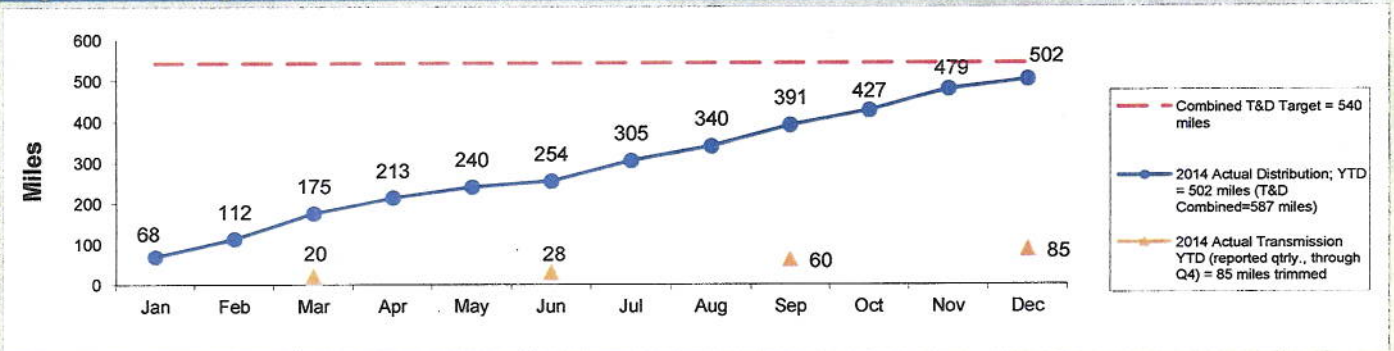
SAIDI - Cumulative



SAIFI - Cumulative

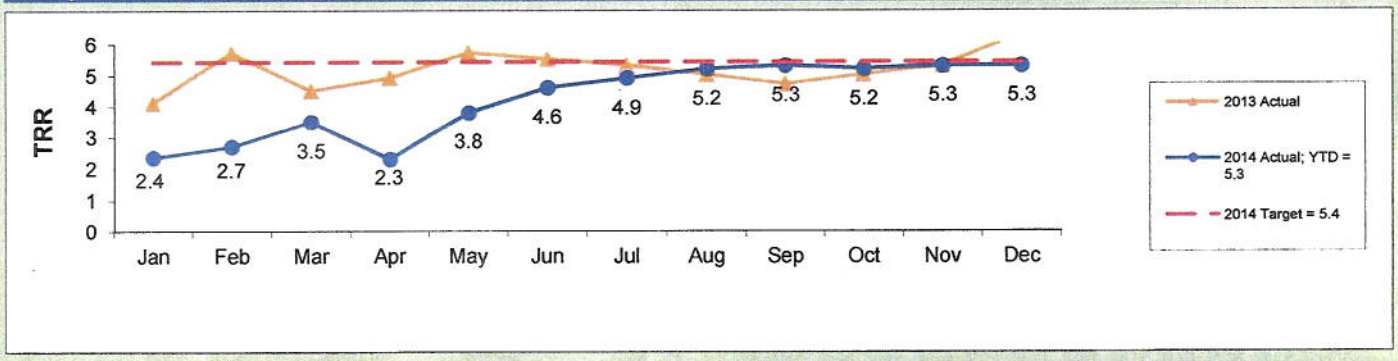


Vegetation Management - Cumulative Miles of Trees Trimmed

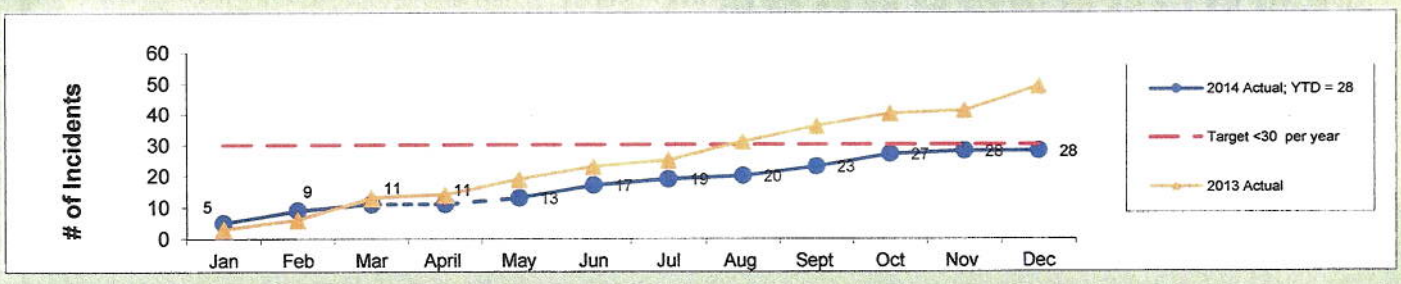


Human Resources:

Safety - Total Recordable Incident Rate (TRR) - Cumulative



Safety - Preventable Vehicle Incidents (Cumulative)



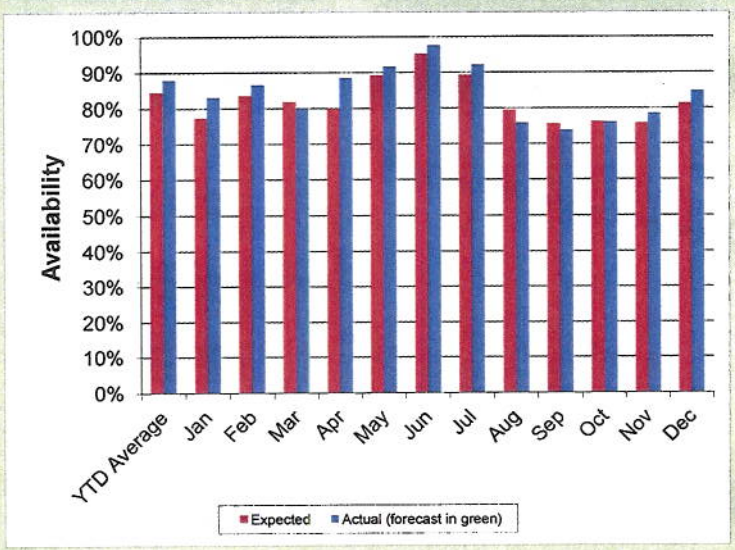
Human Resources:

Hiring Statistics YTD

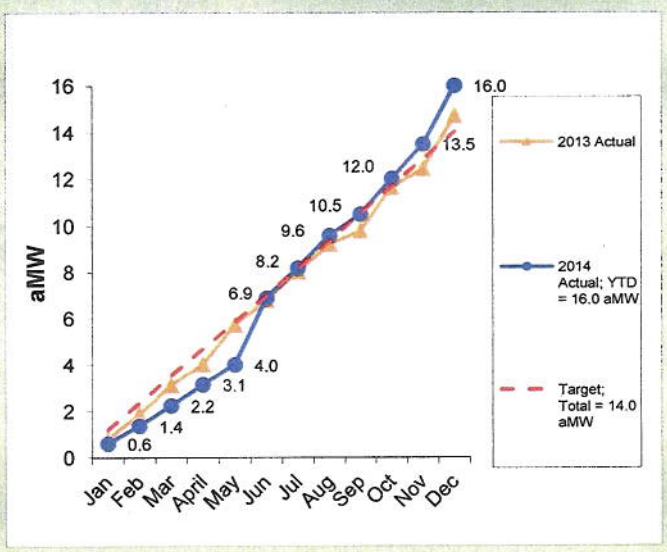
	Jan	Feb	Mar	April	May	Jun	Jul	Aug	Sept	Oct	Nov	Dec
Cumulative # of New Hires	9	26	51	71	87	98	112	125	138	146	153	157
Cumulative # of Promotions	5	9	18	26	38	44	55	64	68	78	82	88
Avg. # Hiring Days for Regular Processes (Goal=45 days)	19	26	18	22	22	22	22	23	23	23	23	24
Cumulative # of Attrition	12	22	34	44	54	65	71	78	83	87	94	103
Vacancy Rate Mo. End (Goal=4.0%)	7.6%	7.0%	6.7%	6.5%	6.2%	6.1%	5.6%	5.5%	5.2%	4.9%	4.9%	5.0%

Power Resources:

Generator Availability-All Units (Actuals %)

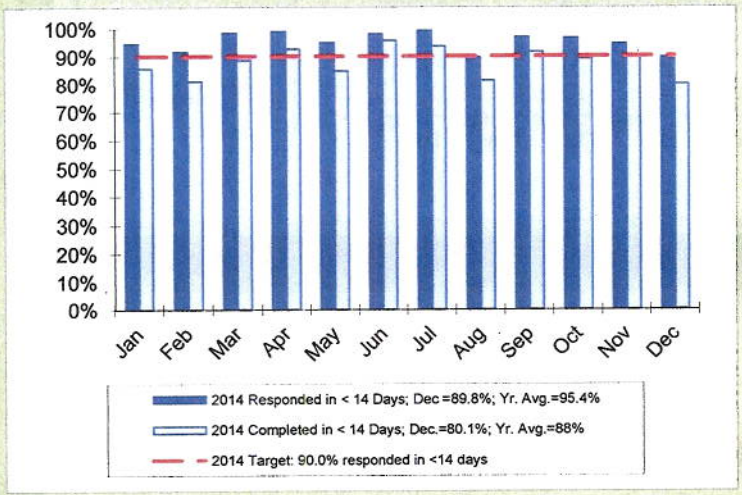
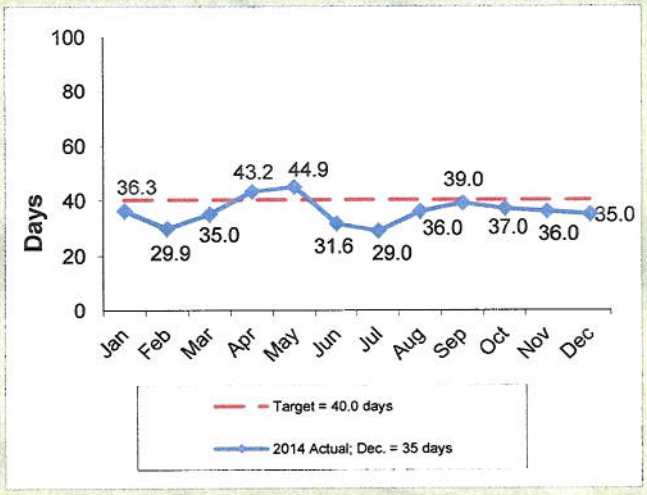


Conservation Savings (Cumulative)



Customer Care:

Streetlight Repairs



Service Connections