



DATE: October 18, 2012

TO: Mayor Michael McGinn
Seattle City Council

FROM: Jorge Carrasco *Jorge Carrasco*

SUBJECT: Financial Update – September 2012

This memo provides an analysis of Seattle City Light's financial condition and operating results through September 30, 2012. The attached Income Statement Analysis, which is summarized in the chart below, provides a summary of how City Light performed year-to-date in 2012 compared to the same period of the previous year and the year-to-date 2012 Financial Plan. In addition, we have provided a forecast of City Light's financial results through December 2012 compared to 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
September 2012
(\$ millions)

	Year-to-date Plan	Year-to-date Actual		Year End Dec. 31		Forecast change from prior month
	2012	2012	2011	Plan	Forecast	
Retail Power Revenues⁽¹⁾	\$ 496.4	\$ 489.1	\$ 482.0	\$ 677.5	\$ 673.3	\$ (2.4)
Net Wholesale Energy Sales⁽²⁾	\$ 81.7	\$ 46.1	\$ 89.1	\$ 102.1	\$ 46.7	\$ (3.3)
Net Power O&M	\$ (185.2)	\$ (173.6)	\$ (156.6)	\$ (253.8)	\$ (257.6)	\$ (0.5)
Net Non-Power O&M	\$ (159.4)	\$ (134.9)	\$ (127.7)	\$ (210.5)	\$ (189.3)	\$ 0.1
RSA Transfers	\$ (0.8)	\$ 33.1	\$ (31.4)	\$ (1.1)	\$ 52.7	\$ 1.8
Taxes & Depreciation & Other	\$ (163.6)	\$ (157.2)	\$ (161.4)	\$ (208.5)	\$ (209.6)	\$ (3.6)
Net Income	\$ 69.0	\$ 102.6	\$ 94.0	\$ 105.6	\$ 116.1	\$ (8.0)
Operating Cash	\$ 220.8	\$ 186.2	\$ 184.1	\$ 163.4	\$ 197.6	\$ (8.2)
Surety Bond Replacement Fund	\$ 10.0	\$ -	\$ -	\$ 20.0	\$ -	\$ -
Construction Account - Restricted	\$ 20.4	\$ 168.2	\$ 113.2	\$ -	\$ 57.8	\$ 21.9
Rate Stabilization Account	\$ 113.5	\$ 108.4	\$ 110.7	\$ 113.8	\$ 88.8	\$ (1.8)
Bond Reserve⁽³⁾	\$ 3.7	\$ 34.1	\$ 1.5	\$ 3.7	\$ 35.0	\$ -
Total Cash	\$ 358.4	\$ 496.9	\$ 409.5	\$ 281.0	\$ 379.1	\$ 11.9
Debt Coverage Ratio	n/a	n/a	n/a	1.8	2.0	(0.02)
Debt to Capitalization Ratio	62.7%	63.0%	64.0%	61.8%	61.2%	0.1%

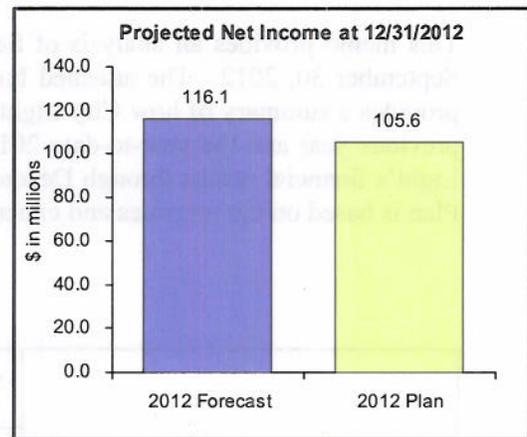
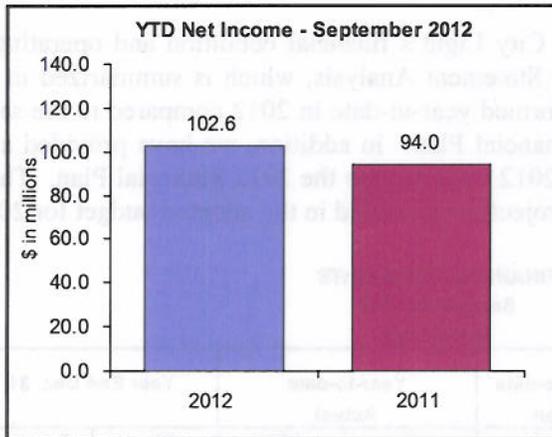
(1) Retail Power Revenues include revenues such as Green Power Program and Power Factor Charges and exclude low-income Rate Discounts.

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

(3) Funds from the Surety Bond Replacement Fund were moved to the Bond Reserve Account on June 1, 2012.

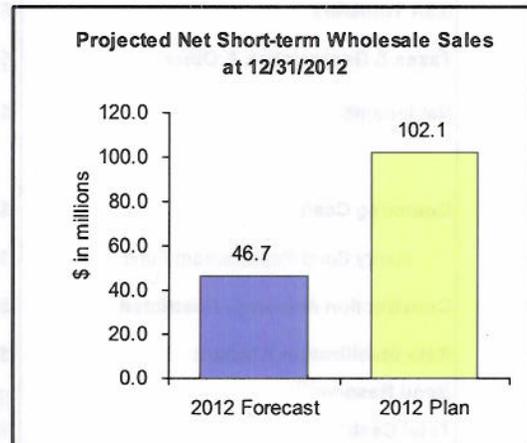
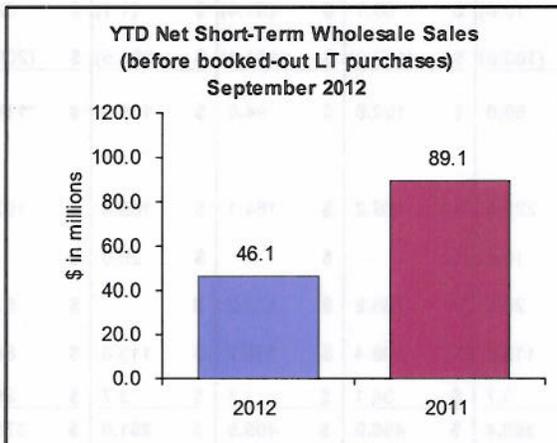
Net Income

As indicated in the table on the previous page and in the charts below, net income for the period ending September 30, 2012 was \$102.6 million, which is an \$8.6 million or 9.1% increase over the same time period in 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 higher capital contributions year-to-date. Offsetting factors include higher generation, long-term contracts and administrative and general expenses and lower power-related revenues.



Projected net income at year-end December 31, 2012 is expected to be \$116.1 million, which is \$10.5 million or 9.9% higher than the 2012 Plan. This difference is due to lower than planned operating expenses year-to-date and reassignment of transmission costs for the Lucky Peak project to the buyer.

Net Short-Term Wholesale Energy

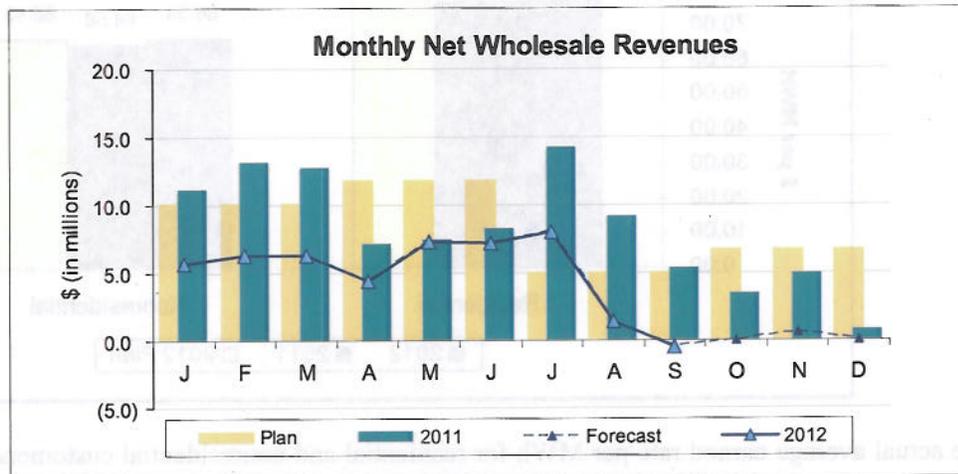


The projections of net short-term wholesale energy sales change weekly due to changes in water conditions, economic factors such as the price of natural gas, system load and the availability of surplus energy for resale. The chart on the next page represents the current forecast for net short-term wholesale revenues before booked-out long-term purchases, which is expected to be \$46.7 million.

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 current forecast is based on much lower energy prices than the historical average and lower energy surplus available for sale.

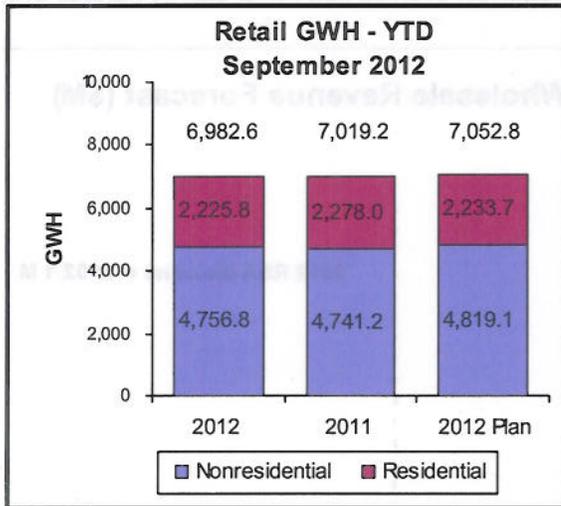


Net wholesale revenues in September 2012 were (\$0.5) million, \$5.9 million lower than in September 2011. September 2011 was a great month for Seattle City Light, unlike September this year. The 220 MW surplus in 2011 was coupled with robust prices. This September, region wide dry conditions meant a slight deficit of 13 MW for SCL. This deficit was anticipated and was offset by month-ahead purchases.



Retail Power Revenues

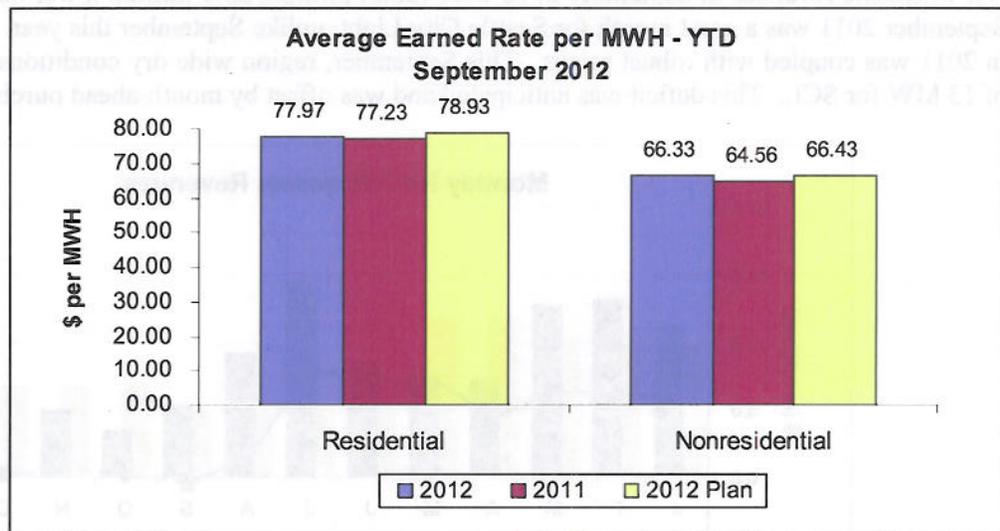
The charts that follow present selected data on year-to-date retail power revenues.



	Retail MWh YTD		
	Nonresidential	Residential	Total
2012 vs 2011	0%	-2%	-1%
2012 vs Plan	-1%	0%	-1%

	Retail Revenue YTD		
	Nonresidential	Residential	Total
2012 vs 2011	3%	-1%	1%
2012 vs Plan	-1%	-2%	-1%

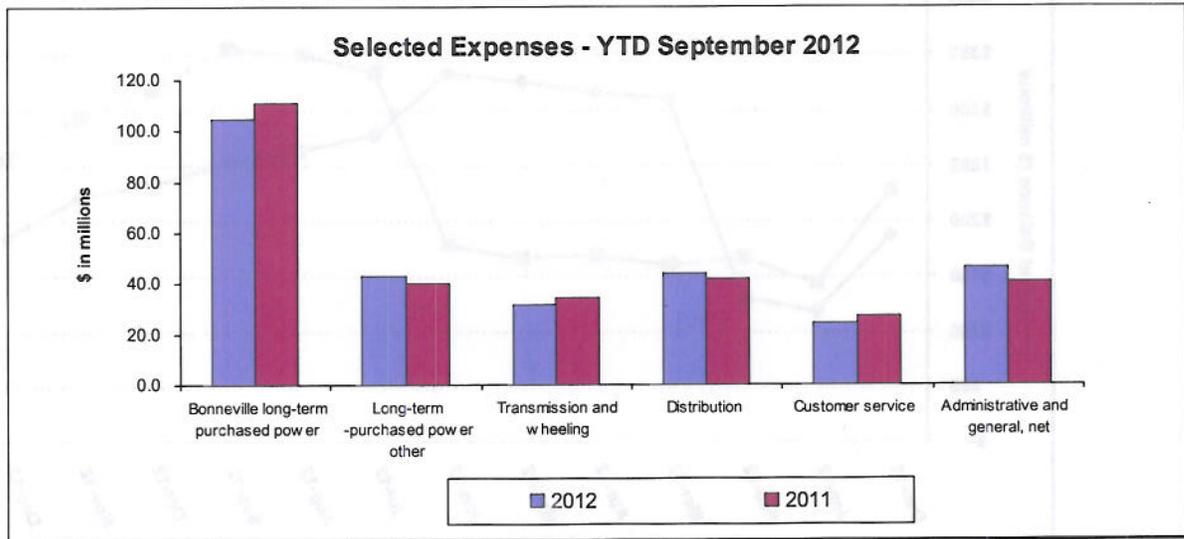
Year-to-date retail revenues are \$7.1 million higher than 2011 primarily due to the across-the-board 3.2% rate increase effective January 1, 2012 and slightly higher non-residential consumption. Offsetting this is lower residential consumption year-to-date. Compared to the 2012 Plan both total electricity consumption and retail revenues are down year-to-date.



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

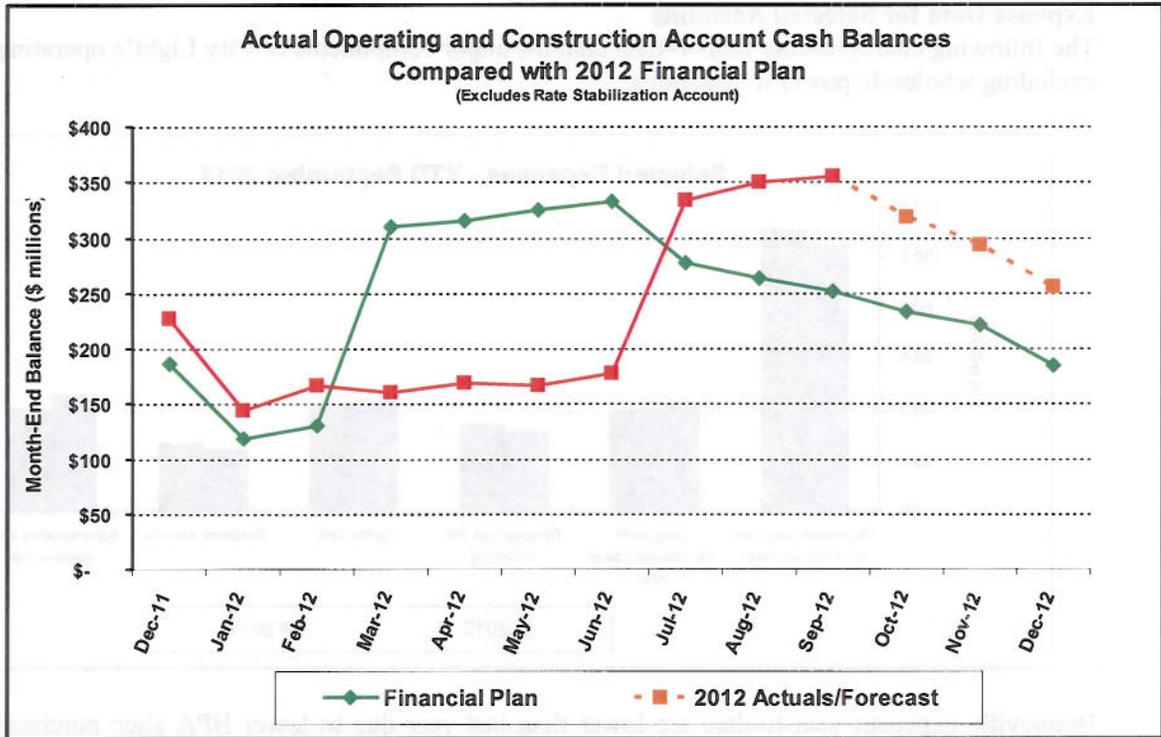
The following chart presents year-to-date data for major components of City Light’s operating expenses excluding wholesale power transactions.



Bonneville expenses year-to-date are lower than last year due to lower BPA slice purchases year-to-date. Offsetting factors are lower BPA Slice true-up credit and higher BPA block purchases. Year-to-date long-term purchased power expenses are higher primarily due to higher purchases from GCPHA and Staline Wind projects. Year-to-date transmission expenses are lower than during the same period last year due to a reassignment of transmission costs for the Lucky Peak project to the buyer in 2012. Distribution expenses are higher year-to-date because of increased efforts dedicated to inspection and replacement of overhead distribution lines. Customer service expenses are lower this year due to lower expense for bad debt. Administrative and general expenses are higher this year primarily due to increases in salary expenses caused by COLAs and lower vacancy rates.

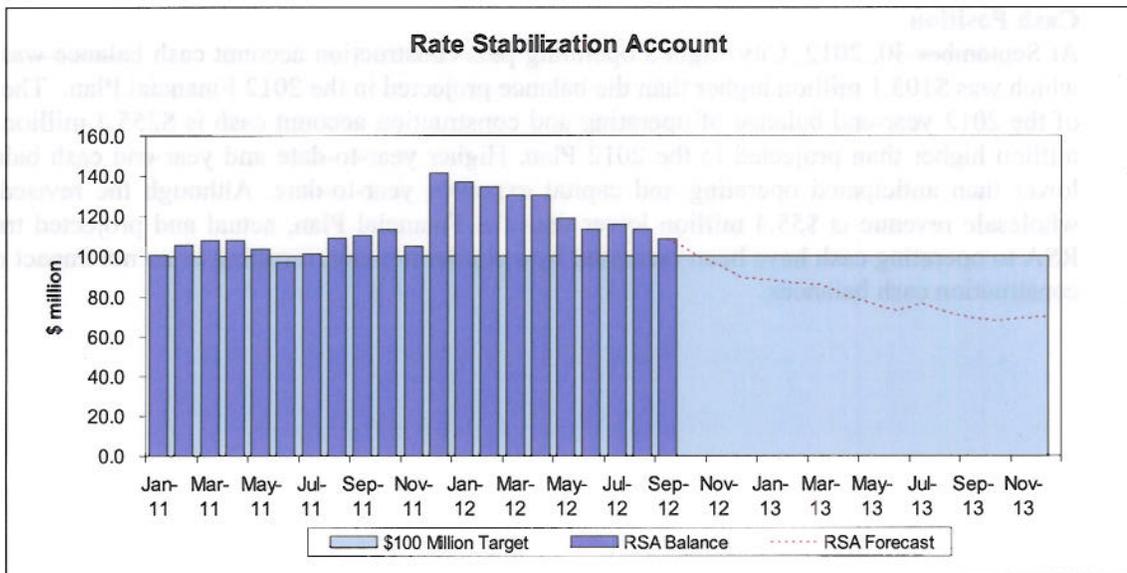
Cash Position

At September 30, 2012, City Light’s operating plus construction account cash balance was \$354.4 million, which was \$103.1 million higher than the balance projected in the 2012 Financial Plan. The revised forecast of the 2012 year-end balance of operating and construction account cash is \$255.3 million, which is \$71.9 million higher than projected in the 2012 Plan. Higher year-to-date and year-end cash balances are due to lower than anticipated operating and capital expenses year-to-date. Although the revised forecast of net wholesale revenue is \$55.4 million lower than the Financial Plan, actual and projected transfers from the RSA to operating cash have been increased by a similar amount, resulting in no net impact on operating and construction cash balances.



RSA Position

The chart below displays the cash balance in the RSA as of September 30, 2012. The Department has been transferring funds from the RSA to supplement lower than expected Net Wholesale Revenues year-to-date, and as of October 5, the year-end RSA balance is projected to be \$88.8 million. This year-end amount would result in the implementation of an automatic 1.5% surcharge on retail rates as of February 1, 2013, unless steps are taken to increase the RSA balance to an amount above \$90 million by depositing additional cash into the account before year end. There will be no RSA surcharge in 2012.



2012 Budget

As of September 2012, City Light is projecting that overall it will be within its budget authority through year-end 2012. The Department has spent 69% of the overall O&M budget (O&M budget includes Non-Power O&M expenses, Purchased Power, Taxes and Debt Service) through September. At this point in the year we would normally expect to have spent 75% of the annual budget. City Light's spending on the Capital program through September is 91% of the 2012 work plan for the year-to-date. City Light forecasts that the accomplishment rate will be approximately 90% by year-end.

Debt-to-Capitalization

At September 30, 2012, City Light's debt-to-capitalization ratio was 63.0%, a decrease from 64.0% this time last year and reported at December 31, 2011. Based on the revised forecast, the 2012 year-end debt-to-capitalization ratio is now expected to be 61.2%, slightly lower than the 2012 Plan.

Compliance with Risk Policies and Standards

Attached for your information is the City Light Risk Oversight Status Report as of October 3, 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 September 2012, with 2011 data included for comparison, is attached.

Attachments

Line No.	Condensed Statements of Revenues and Expenses	Year-to-date			Year Ending December 31, 2012		
		[A] Actuals September 30, 2012	[B] Actuals September 30, 2011	[A - B] Actuals to Actuals Variance	[C] 2012 Revised Forecast	[D] 2012 Financial Plan	[C - D]
1	Unaudited						
2	In millions						
3							
4							
5	Operating Revenues						
6	Retail power revenues	\$ 489.1	\$ 482.0	\$ 7.1	\$ 673.3	\$ 677.5	(4.2)
7	Short-term wholesale power revenues, net (lines 41 + 44)	47.9	88.1	(40.2)	57.3	146.1	(88.8)
8	Power-related revenues - other	22.1	48.7	(26.6)	15.8	35.9	(20.2)
9	Transfers from/(to) rate stabilization account	33.1	(31.4)	64.5	52.7	(1.1)	53.8
10	Other revenues	17.5	16.9	0.6	23.1	22.2	0.8
11	Total operating revenues	609.7	604.3	5.4	822.1	880.6	(58.6)
12	Operating Expenses						
13	Generation	22.7	21.2	1.5	31.3	39.1	(7.7)
14	Bonneville long-term purchased power	104.7	110.7	(6.0)	148.9	150.8	(1.9)
15	Long-term purchased power - other	42.8	40.2	2.6	55.9	65.8	(10.0)
16	Short-term wholesale power purchases	5.5	4.5	1.0	15.4	49.1	(33.7)
17	Power-related wholesale purchases - other	5.5	7.0	(1.5)	7.4	7.3	0.0
18	Other power costs	7.3	7.1	0.2	10.1	11.8	(1.7)
19	Transmission and wheeling	31.7	34.8	(3.1)	46.4	49.0	(2.6)
20	Distribution	44.1	41.7	2.4	62.9	68.0	(5.1)
21	Customer service	24.4	27.1	(2.7)	34.0	36.7	(2.7)
22	Conservation	14.7	13.7	1.0	22.3	27.7	(5.4)
23	Administrative and general, net	46.5	40.9	5.6	61.9	61.4	0.5
24	Taxes	55.6	54.2	1.4	76.5	77.6	(1.2)
25	Depreciation and amortization	69.8	66.2	3.6	95.5	89.7	5.8
26	Total operating expenses	475.3	469.3	6.0	668.3	733.8	(65.5)
27							
28	Net Operating Income	134.4	135.0	(0.6)	153.8	146.8	7.0
29							
30	Other Deductions, Net						
31	Investment income	4.3	3.8	0.5	5.4	5.4	0.1
32	Other income (expense), net	1.7	2.8	(1.1)	3.2	5.7	(2.6)
33	Interest expense	(57.4)	(56.6)	(0.8)	(86.4)	(100.4)	14.0
34	Noncapital grants	2.4	1.6	0.8	6.0	3.9	2.1
35	Capital contributions	16.7	7.4	9.3	33.2	43.7	(10.5)
36	Capital grants	0.5	-	0.5	1.0	0.5	0.5
37	Total other deductions, net	(31.8)	(41.0)	9.2	(37.7)	(41.2)	3.5
38							
39	Net Income	102.6	94.0	8.6	116.1	105.6	10.5
40	Note A:						
41	Short-term wholesale energy sales, gross	51.6	93.6	(42.0)	62.2	151.2	(89.0)
42	Short-term wholesale energy purchases	(5.5)	(4.5)	(1.0)	(15.4)	(49.1)	33.7
43	Net ST wholesale sales before booked-out LT purchases	46.1	89.1	(43.0)	46.7	102.1	(55.4)
44	Booked-out long term purchases	(3.7)	(5.5)	1.8	(4.9)	(5.1)	0.2
45	Net short-term wholesale energy sales	42.4	83.6	(41.2)	41.9	97.0	(55.1)
46	Note B:						
47	Power-related revenues, net (line 8 minus line 17)	16.6	41.7	(25.1)	8.4	28.6	(20.2)

**Net Income Variance Analysis
September 2012**

Variance Year-to-Date 2012 Compared to 2011 Actuals: \$8.6 million or 9.1%

Major components (\$ millions):

\$94.0	Net Income YTD through September 30, 2011
\$7.1	Higher retail revenues due to 3.2% rate increase effective January 1, 2012 and slightly higher consumption by non-residential customers
(\$43.0)	Lower net surplus energy sales due to lower energy surplus and lower energy prices
\$64.5	RSA deferred revenues transferred-in
(\$25.1)	Lower power-related revenues, net, reflects (\$20.6) million lower cash revenue and (\$4.5) million lower noncash revenue (primarily fair valuation of power exchanges)
\$6.0	Lower BPA purchased power
\$2.7	Lower customer service expenses due to lower bad debt expense
(\$5.6)	Higher A&G, net
(\$3.6)	Higher depreciation and amortization
\$9.3	Higher capital contributions
(\$3.7)	Other (net)
\$102.6	Net Income YTD through September 30, 2012

Variance 2012 Revised Forecast Compared to Financial Plan: \$10.5 million or 9.9%

Major components (\$ millions):

\$105.6	Net Income YTD through December 31, 2012 - Financial Plan
(\$55.4)	Lower net surplus energy sales than planned
\$53.8	Transfer from RSA to offset lower net surplus energy sales
\$7.7	Lower generation expenses
\$5.1	Lower distribution expenses
\$5.4	Lower conservation expenses
(\$5.8)	Higher depreciation and amortization
\$14.0	Lower interest expense
(\$10.5)	Lower capital contributions
(\$3.8)	Other (net)
\$116.1	Net Income YTD through December 31, 2012 - Revised Forecast



City Light Risk Oversight Status Report

As Of Wednesday, October 3, 2012

Summary

	<u>% of 5 yr Avg</u>	<u>Current '12 Avg</u>	<u>5 Yr Avg</u>
SCL Hydro Generation	96%	1,068 MW	1,115 MW
Peak Market Prices	53%	\$23.46	\$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.

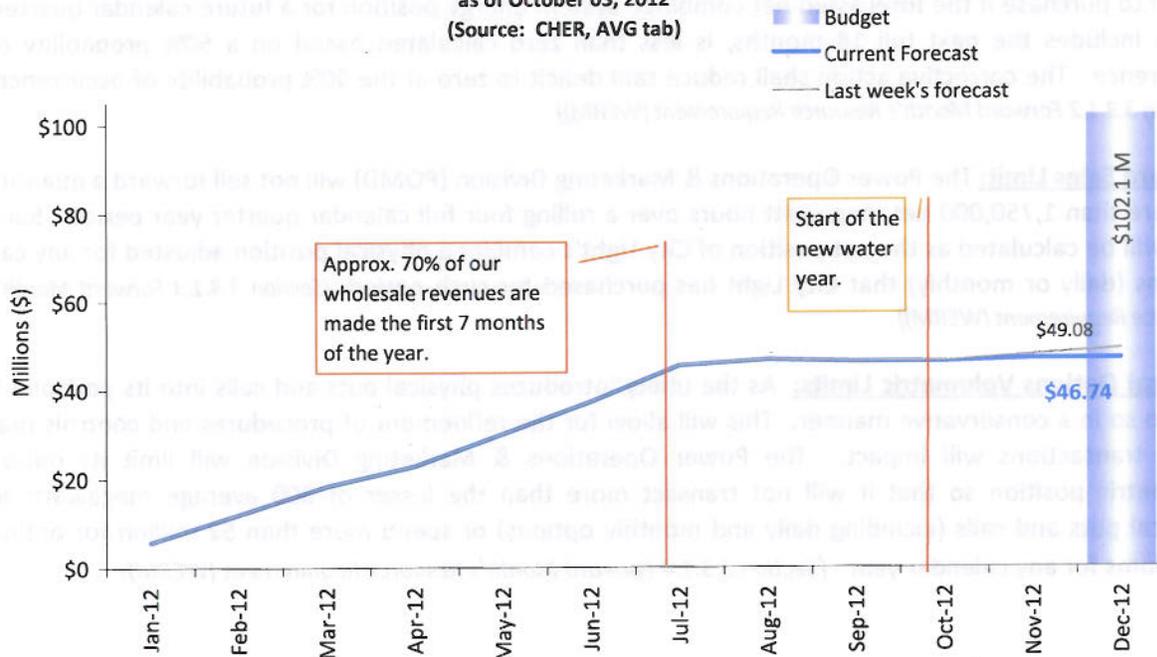
Peak Market Prices: The average peak market price for the nearest electricity trading hub (Mid-C) for the 2012 calendar year. The 2012 average is comprised of monthly peak forward marks for future months and averaged Dow Jones firm peak index daily prices for past months. The 5 year average is calculated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

Wholesale Revenue Variance: In the 2012 approved budget, the approved Wholesale Revenue is \$102.1 million. The chart (Chart 1) compares the current annual approved budget (\$102.1 million) with the current forecast of \$46.7 M with a 90% confidence level of \$41.43 M and a 10% confidence level of \$52.33 M. The Net Wholesale Revenue (NWR) decreased by \$2.7 M from the previous CHER run as a result of decrease in resources accounting for \$2.7 M, decrease in estimated October net revenue of \$0.2 M and increase in prices accounting for \$0.5 M.

Chart 1

Cumulative Net Wholesale Revenue for 2012

**Budget vs. Forecast
as of October 03, 2012
(Source: CHER, AVG tab)**



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

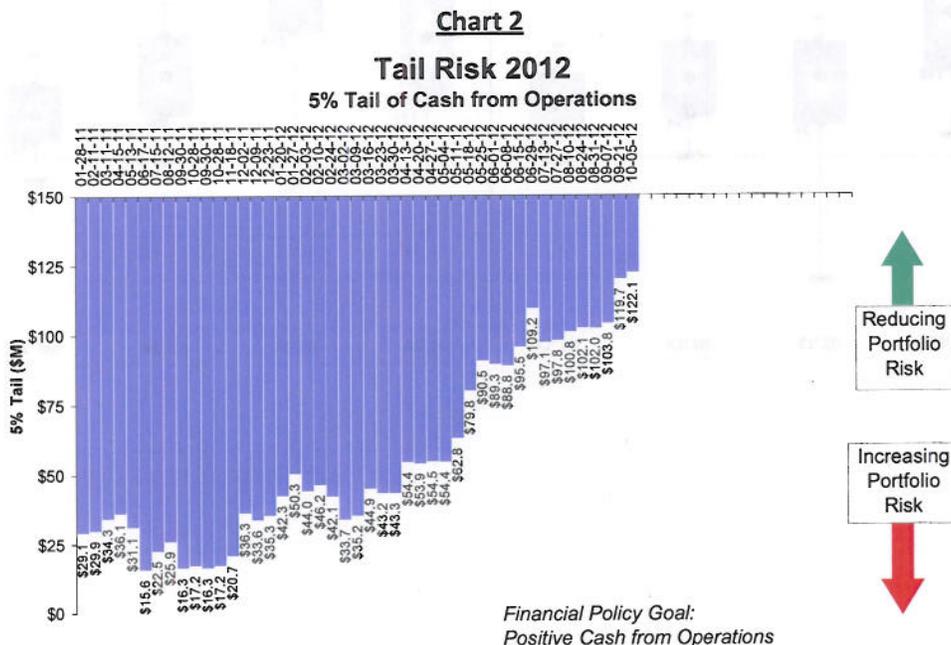
In October 2007, City Light implemented a risk metric named the “5% Tail Risk”. It is calculated as the average of the worst-case scenarios for City Light’s cash from operations for the calendar year. Cash from operations is a bottom-line financial metric defined as the cash available to finance capital 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 \$122.1 million of Cash from Operations.

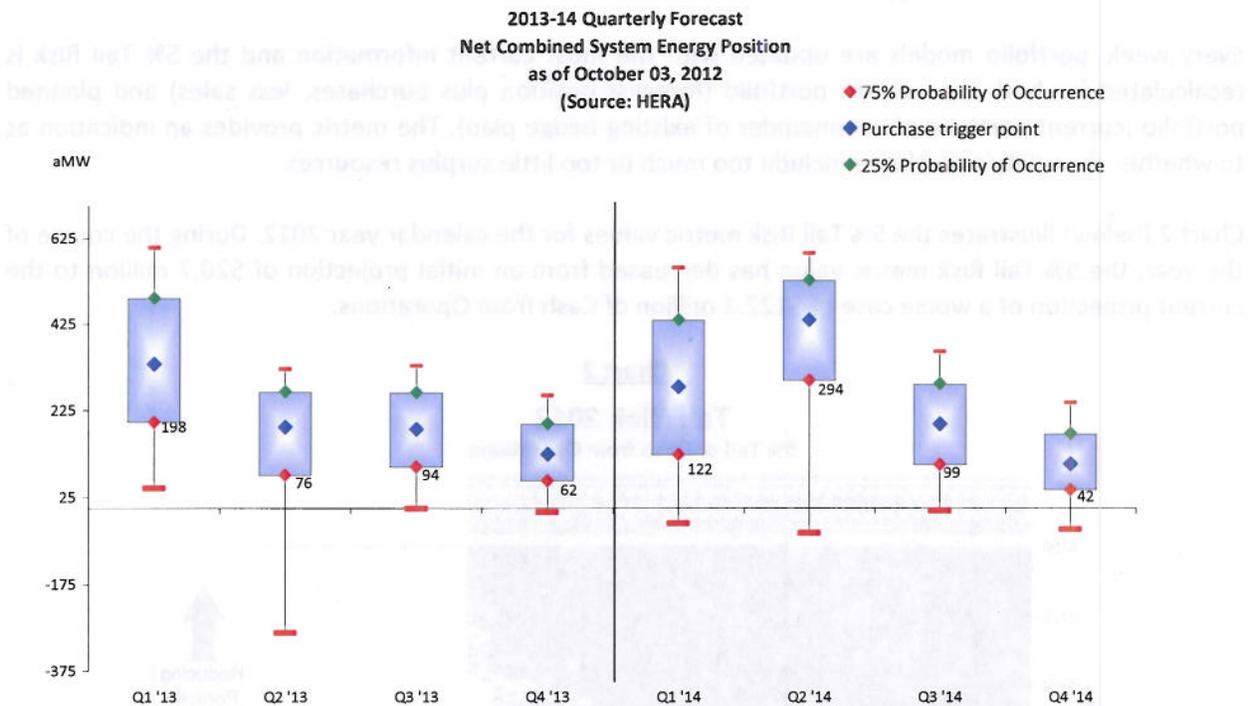


Hedging Plan & Position Status

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

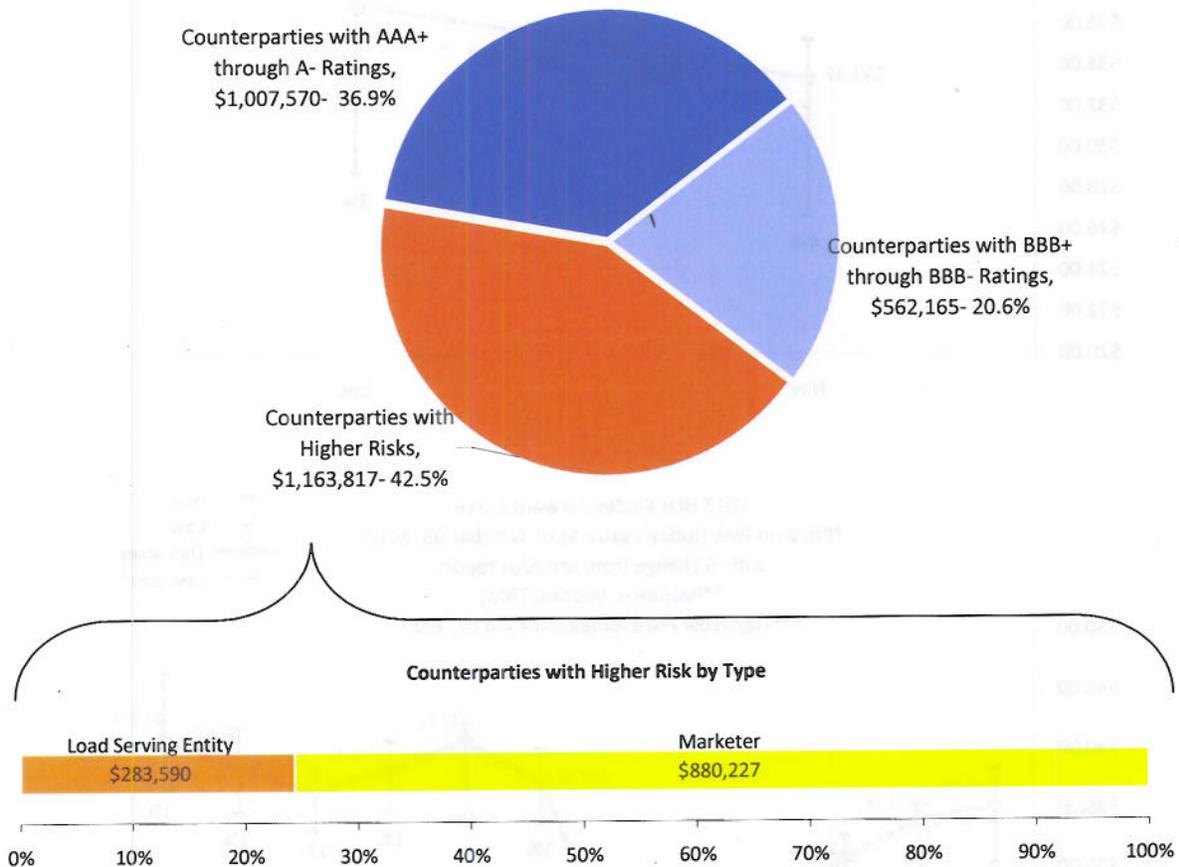


Credit

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

**Total Net Credit Exposure by Implied Ratings Class
as of October 03, 2012**



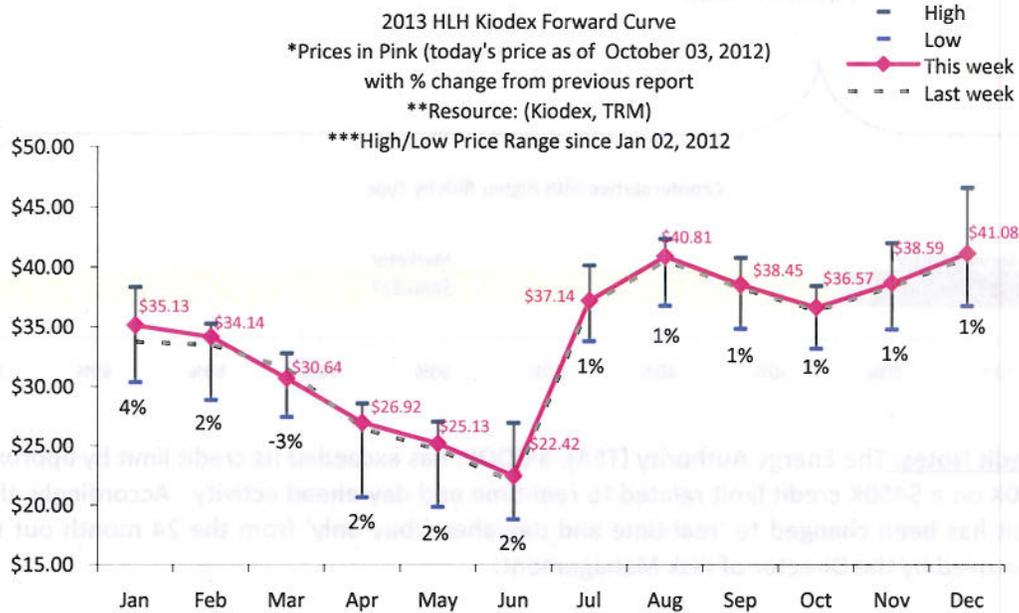
- Credit Notes:** The Energy Authority (TEA), a COOP, has exceeded its credit limit by approximately \$30K on a \$450K credit limit related to real-time and day-ahead activity. Accordingly, the tenor limit has been changed to 'real-time and day-ahead buy only' from the 24 month out tenor as approved by the Director of Risk Management.

TEA is in the process of considering advance paying on amounts due for September and October transactions. Risk will know more on this possibility early next week. TEA is among SCL's oldest counterparties and has a good payment history. Risk is in the process of reviewing TEA.

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 the upcoming 12 months since the beginning of January 2012.

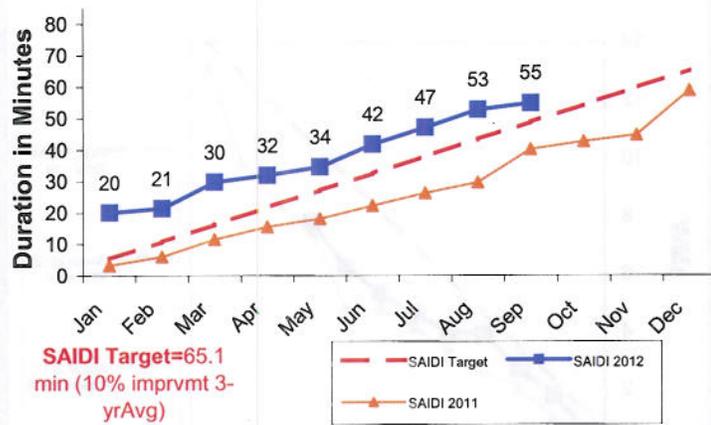
Chart 5



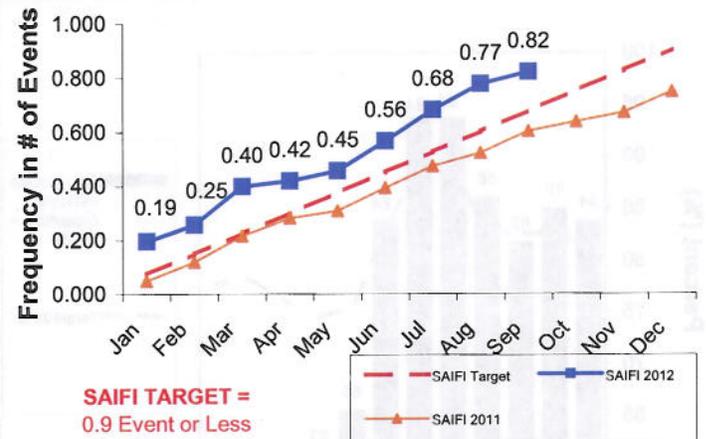


Distribution Operations:

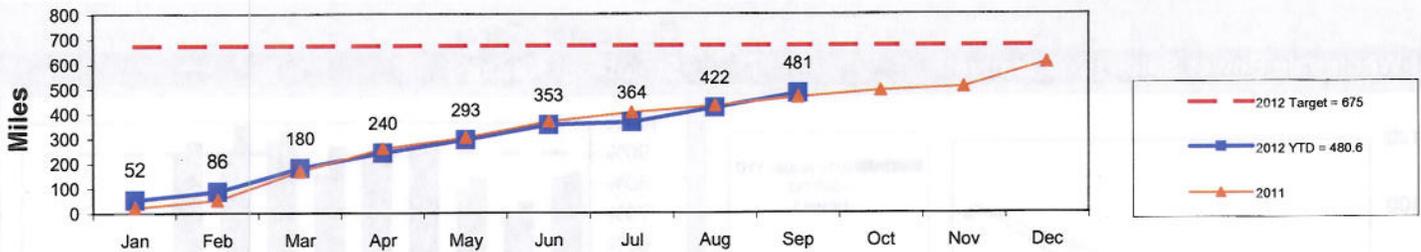
SAIDI - Cumulative



SAIFI - Cumulative

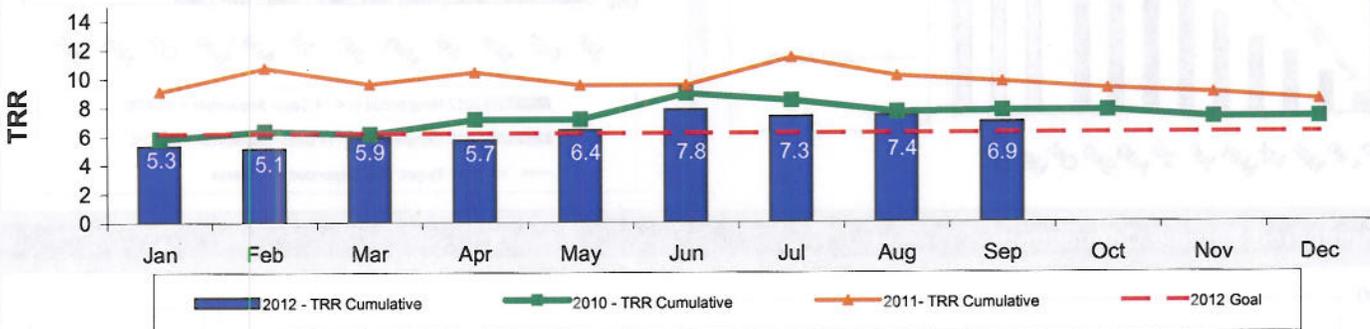


Vegetation Management - Cumulative Miles of Trees Trimmed



Human Resources:

Safety - Total Recordable Incident Rate (TRR) - Cumulative



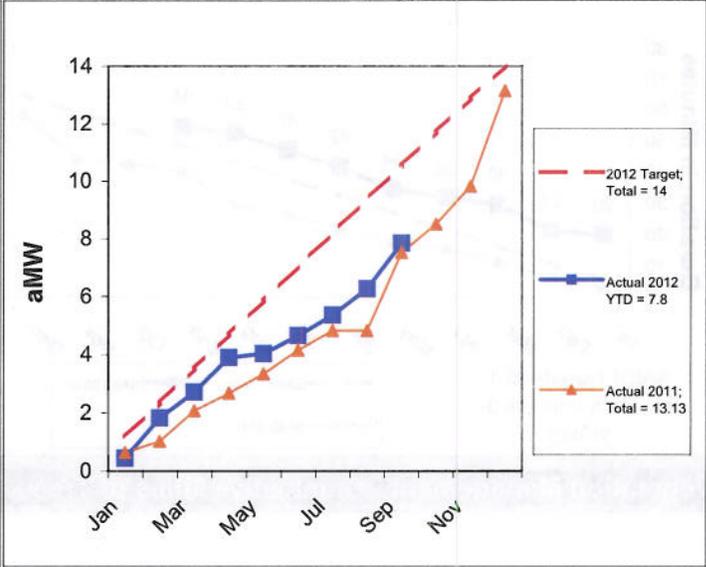
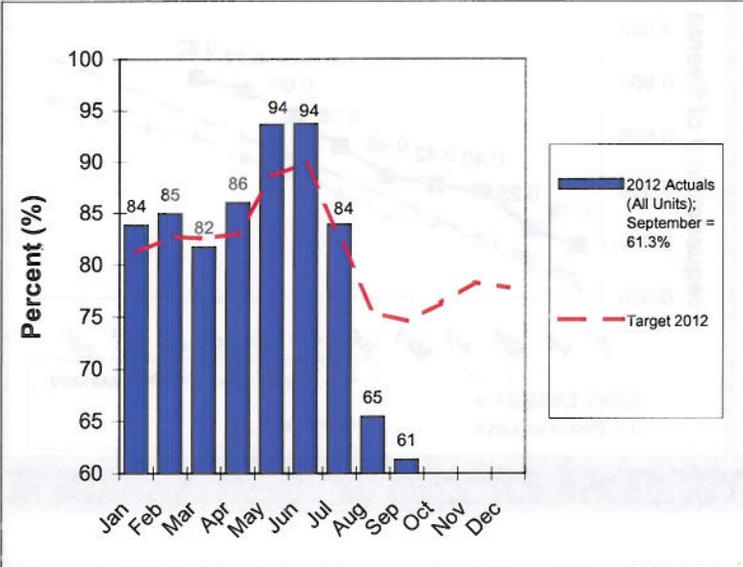
Hiring Statistics YTD

	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			
Cumulative # of Promotions	5	12	12	18	20	21	22	27	36			
Ave. # of Hiring Days	47	47	46	48	52	52	54	54	55			
Cumulative # of Attrition	8	15	24	33	41	49	60	73	79			
Vacancy Rate Mo. End	7.8%	7.3%	7.4%	7.3%	7.0%	7.3%	7.4%	7.6%	7.3%			

Power Resources:

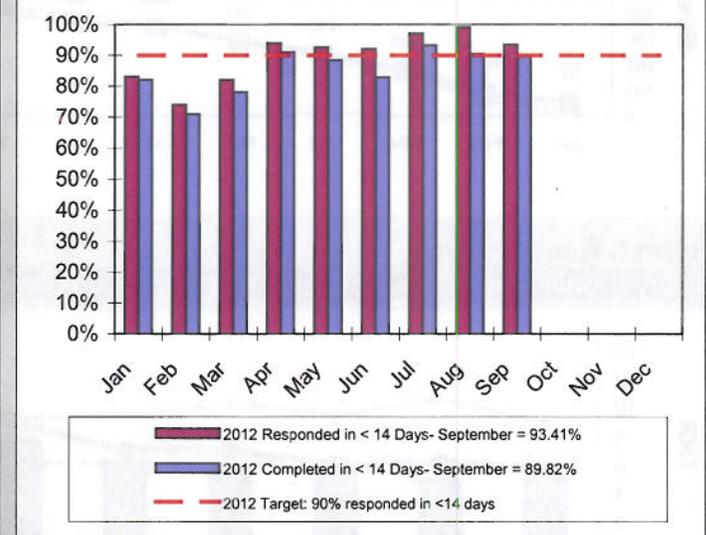
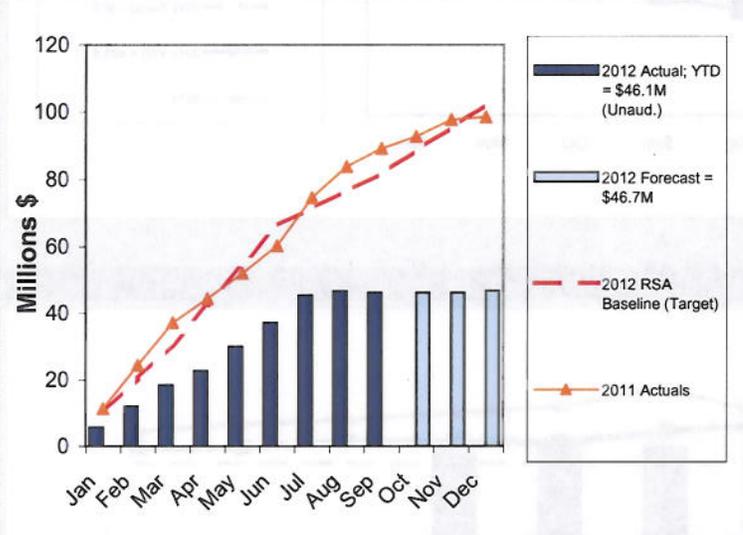
Generator Availability-All Units (Actuals %)

Conservation Savings (Cumulative)



Net Wholesale Power Sales (Cumulative)

**Customer Care:
Streetlight Repairs**



Non-Engineered Service Connections

