

Gary Zarker
City Council Reconfirmation Questions

February 14, 2003

I. Vision, Mission, Strategies

What are the greatest challenges you see for the utility in the next four years and what are your major goals for City Light during this time period and beyond? When and how will you achieve them?

We start from a very solid foundation. Our large generating systems are in better shape now than they have been in many years with the completion of the seven-year rehabilitation of our largest hydro plant, Boundary. We also have a competitive resource portfolio that will provide sufficient power for our customers' needs in nearly all water conditions through the rest of the decade. Our new financial policies are in place, and we should be able to meet the targets of that plan sometime in 2004.

At the same time, we are walking on shaky ground. The electricity industry, by and large, is in shambles. Private companies that leaped into the deregulated world have lost 85% of their market value—over \$290 billion. And the worst is not over; a host of projects they started are now stalled as more than \$80 billion in short term financings are coming due. The ripple effects of these failures continue to plague the industry. The Bonneville Power Administration, hit hardest in the energy crisis, is now confronted with another bad water year and another major rate increase that many of its customers feel they cannot pay. The President's budget has made the most explicit attack on Northwest preference for Bonneville power that we have seen in decades. Moreover, the federal government continues its deregulation agenda with the country deeply divided along regional lines. An industry that thrives on certainty is struggling with the deepest doubts – the economy, the regulatory environment, and its very credibility.

Here at home, we face serious challenges from any economic scenario—an improving economy or one that continues to stagnate. Strong growth leads to more demands on our distribution system. Continued slow growth erodes our revenues. Clearly over the last couple of years, the Northwest has lost ground on the competitive advantage its electricity system provided for our regional economy, but the losses to date could easily pale in comparison with the threats immediately before us.

In this context, I want to answer your question about my goals in the next four years.

- Create a long term financial strategy that provides stability, predictability and opportunity for our customers.
- Engage our elected officials and our customers in the effort to keep the Northwest's unique energy system cost-based and under local and state control.
- Restore employee morale.

First, we have to complete the energy crisis financial recovery strategy we all set for the utility. The goals are not just to repay the debt, establish a cash reserve, and retire some of the rate surcharges. Our more robust power supply and new financial policies will accomplish these immediate goals next year. **The broader goal is to establish a long-term financial strategy that will support the service and economic needs the community expects of its municipally owned utility.** The City Council already has in its work program many of the elements of the comprehensive strategic planning process that can help formulate these policies. We will be working with you on an assessment of the reliability challenges our distribution system faces as growth consumes capacity on our system. The strategic business planning process will engage a broad cross section of the community in a dialogue about expectations and strategies for success in an unstable and unpredictable environment. We will continue our review of the power resource plan with you. These work elements and many others should set a strong context for the critical long-term decisions the City's elected officials will need to make next year when we have put the effects of the 2000-2001 energy crisis fully behind us.

There is no question in my mind that the great legacy of public power in Seattle, the Northwest, and our country is threatened as never before. **We have to find a way to engage our community in a dialogue about the terribly complex issues that revolve around our utility.** We need to come up with a well-informed strategy for preserving the low cost-based rates, for keeping our environmental principles strong, and for making our customer service standards the best they can be. The Federal Energy Regulatory Commission's schemes for restructuring the national electricity industry, mandated changes in the governance and operation of the Region's high voltage transmission grid, and the Administration's recent attack on the Bonneville Power Administration are but a few of the challenges public power faces. My task is to engage utility stakeholders and elected officials in a quality discussion of these very difficult and evolving issues that leads to well-informed policy direction that can sustain City Light through this time of upheaval.

Finally, the restoration of employee morale is a key objective. The brutal insults of the energy crisis, the tidal wave of electricity restructuring initiatives, and continuing financial restraint – all in the glare of critical press coverage – have taken a toll on morale. Seattle City Light is a well respected, national leader in the electricity industry because we have a great group of employees working for us. They are dealing with more change than ever at a time when we are asking them to do more with less. I am very proud of their response and their accomplishments. City Light's leadership has a big challenge before it. We have to provide our employees with better communications about the state of our industry, provide better training and tools that enable our employees to perform effectively, and we must demonstrate to them that we appreciate their effort and accomplishments.

2. What were your goals when you were appointed as Superintendent of City Light in 1994 and how do you view your progress in meeting those expectations you set eight years ago?

I stated three goals when I came to the utility in 1994:

- Establish a confident and effective workforce.
- Establish and begin implementing the direction the City wants the utility to play in this rapidly changing industry.
- Get firm control of our resources.

Confidence – When Mayor Rice asked me to lead the utility eight years ago, his challenge was quite clear. He wanted me to focus on culture issues that clearly were damaging utility performance. I found a utility workforce that was ready and eager to put those issues behind it. We worked hard on employee communications, emphasized our expectations for a respectful work environment, and made people accountable. Today, I believe we have made tremendous progress in meeting Mayor Rice’s challenge. Not only are the statistics good, but there is a genuine commitment to the goal. It’s a goal we’ll never be finished with, but I am very proud of the accomplishments City Light has made in this regard.

Eight years ago, I also promised to create a better working relationship with the rest of the City family. Again, I think the progress has been strong. We are actively engaged in neighborhood planning and in construction coordination. We have a much closer relationship with Seattle Public Utilities that is benefiting the customers of both utilities. We play important support roles in many of the critical transportation initiatives our City is engaged in. Our support of the Arts Commission’s one percent for art collection is thriving. City Light can be counted on to be a strong contributor to major City initiatives rather than an aloof and disinterested player. One of our greatest strengths as a public utility is our connection to the broader goals and services of our City. City Light is better for it. The City is better for it.

I also mentioned the customer connection to our confidence goal eight years ago. We have had some challenges with our billing system, no doubt about that. We are working hard to learn from those mistakes, correct the problems and meet fundamental expectations for accurate and timely billings. We’ve made substantial progress after a tough start. The important thing to remember about the billing system is that it is the platform on which rests many other services our customers want us to provide. The key accounts function we established early on is working very well. A handful of account

Executives establish close partnerships with some of our most critical customers. We have good working relationships with community services for low-income customers and those needing special utility services, and we are proud of our outreach during the energy crisis. The improved customer service ethic is also evident in the very creative work our service engineers carried out working with developers through a period of tremendous economic growth. Last year's billing glitches aside, we've we have made good progress towards the goal of being a customer focused municipal utility.

The last area related to confidence I mentioned eight years ago had to do with the relationship with elected officials. On this score, it is apparent to me that we still have a lot of work to do. This is what I said eight years ago:

"Confidence is particularly important with elected officials. This is a very entrepreneurial activity for a municipal government to manage. It may well be getting even more entrepreneurial. We have to get agreement with you about the course you want us to chart and about the limits of our authority. We also need to make sure we are communicating effectively within this framework."

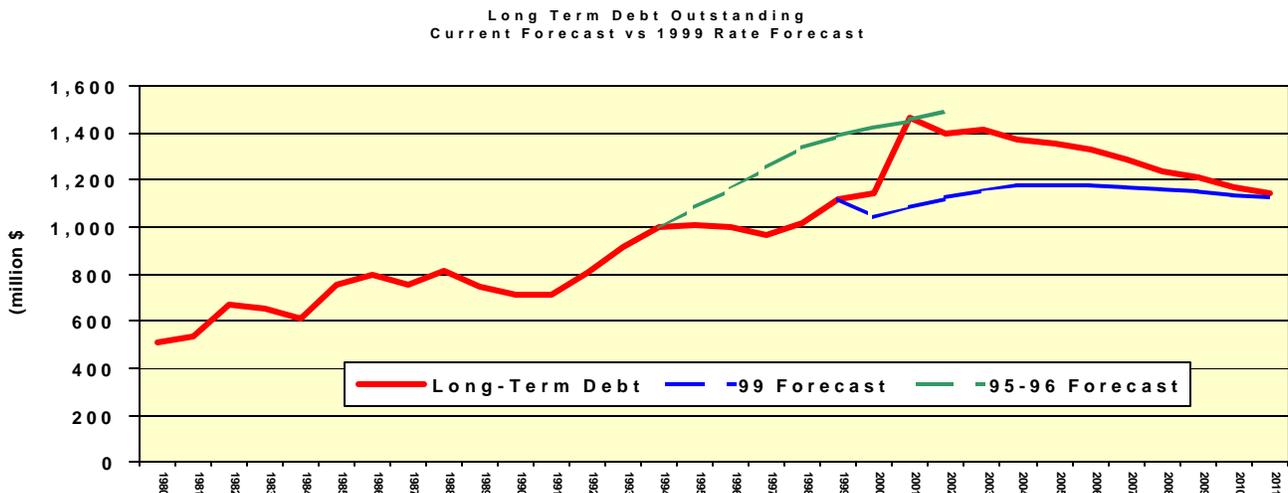
This is as true today as it was eight years ago. City Light's basic service is based on very complex engineering and intricate relationships with a host of external players. We don't control all of the variables that affect our outcomes. And as we have learned all too painfully, the risks can be extreme. All of this would be difficult enough in a stable industry, but we have been working with our elected officials in a world that is turned on its head. Somehow, we have to find a way to communicate more effectively with our elected officials about the shifting complexity of our business so that we all are confident that we have set a direction that will serve our customers' well.

I honestly believe that the men and women of Seattle City Light have been committed to improving communications with elected officials. We are frustrated that our efforts are not producing results you find satisfactory. I am, however, encouraged with changes I see. More elected official staff will help us refine presentations and surface other points of view. The new advisory board should bring more in depth consideration of tough policy issues. Expanded City Council utility committee membership will improve transitions, create a broader base of expertise, and bring more timely oversight of performance. I sincerely welcome all of this. City Light is committed to doing its part. One lesson I hope we all have learned is that we can't let communications problems deteriorate to this point again. I will be staying very close to this issue with you as we go forward.

New Direction – We had a terrific planning process in play from 1996-99 that was unfortunately interrupted by the energy crisis. I think we engaged our employees, elected officials and other stakeholders quite effectively. We were among the first to employ scenario based planning in the industry and that helped us chart a path that seemed to be producing measurable results. When we began the first update in 1998, we began making critical adjustments to the original plan that seemed to be driven by changing events. Unfortunately, the plan did not anticipate the speed with which the West Coast energy crisis overtook us or the failure of federal regulators to do their job of policing the market.

Our strategic business-planning model can work well for us, but we have to make it a living process. I have to keep utility leaders and employees engaged. We need to keep elected officials involved in not only our performance on current goals, but also in the internal and external dynamics that seem to constantly challenge the rules of the game. Oversight is more than just measuring the accomplishment of adopted goals. It involves the regular revisiting of the goals themselves in the light of shifting circumstances. I am hopeful that the new advisory board will be able to play a role in helping us all keep the business planning effort alive and effective.

Resource Control – For many years, in reaction to the financial trauma of the WPPSS experience, it was the policy of the City to use debt to stabilize rates.



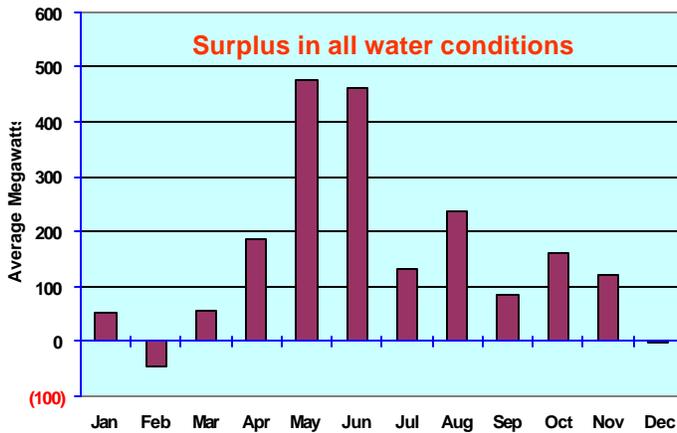
Very early in my tenure as superintendent I realized that it was only a matter of time before the legacy of those debt service payments caught up with our rates and would become the largest driver of new rate increases. At the same time, the RW Beck study I found on my desk when I came to work pointed out some critical deficiencies with our capital plant. With strong City Council engagement, we

turned the focus of the City's policy guidance to making sure the utility had its capital improvement priorities right and that we were getting good value from our new investments. We developed evaluations that assured that we carried the work out in a timely and cost effective manner. And all of this was in the context of new strong message that it would be responsible financial restraint rather than a foolish reliance on our credit card that would guide our future finances.

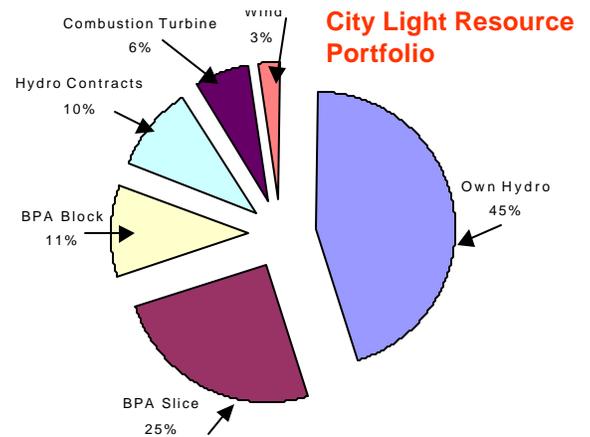
I think the record is clear that the utility embraced this new approach and performed quite well. One of my first priorities was to get overall debt under control, even as we rehabilitated our critical, low cost generation facilities. We brought in outside experts who trained our folks to manage capital projects more effectively. And, all of this produced the desired result of turning the tide on the growth in our outstanding debt rather dramatically. Subsequently and unfortunately, we had to borrow heavily to keep the lights on and ease the energy crisis rate shock. I am confident, however, that the attention we have given to more effective capital planning and debt management will continue to serve us well as we return to our debt reduction focus.

3. Since the energy crisis, what changes have you implemented at City Light and what further steps do you believe are needed to fully restore the Council's and the public's confidence in City Light and in its superintendent?

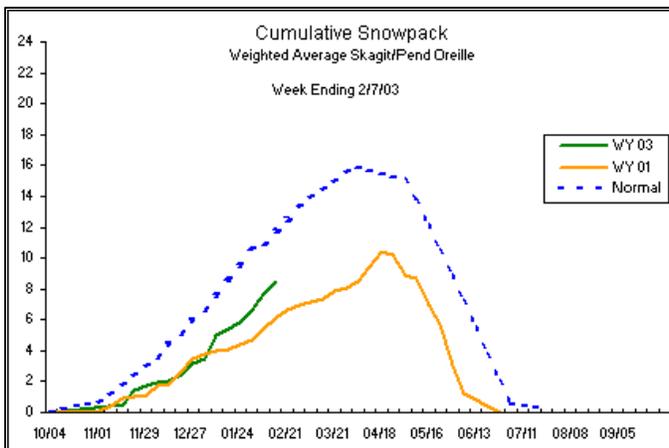
We had a terrific planning confidence is based on our performance and on our demonstrated commitment to improvement. In that regard, I think the changes we have implemented at Seattle City Light are producing the results we have said they would.



The new power resource plan we have now fully implemented is protecting us from reliance on wholesale power markets to meet our service obligations. . The cost of that portfolio is quite competitive in the market we are in and is complementary to our owned hydro resources.



We are being challenged by another drought every bit as bad as the one we dealt with in the winter of 2000-2001 and yet our power supply is secure. We will not make as much revenue from surplus power sales this year as we had hoped, but we are generating enough revenue to assure accomplishment of our financial recovery strategy very close to the schedule we originally predicted.



As our recent update on the Deloitte & Touche audit indicated, we made many improvements to our power and risk management functions very quickly. Those changes are serving us well. The power industry is suffering from a major shakeout. Once reliable trading partners suddenly have become major credit risks, but our counterparty credit risk and contract management approach is protecting the reliability of our payment stream.

We have a skilled group of power traders and planners, many of whom came to us with a great deal of industry experience. We were pleased that the Council's recent audit found the experience and competence of this part of our organization to be strong. We have bolstered our internal planning with the work of a number of outside experts, so our strategies are now better informed by peer review. Reporting on our position is also becoming much more timely and reliable. All of this is helping us refine our critical power and risk management functions.

Finally, our internal oversight and management is collaborative. Weekly risk management meetings bring together key players from several utility branches and City departments – including the City Council staff -- to review our current position and to coordinate responsibilities for establishing our future position. Our planning and project assessment process integrates expertise from across the utility to evaluate new generation and transmission issues and opportunities. This is a continuation of the more collaborative approach that I launched as a new superintendent, but it is now an established way of how we do business. Our power supply and our power management activities are producing excellent benefit for our customers.

There is still much to do. Our power management activities are perhaps too limited by historical practices. We need to complete the RW Beck risk management review as soon as we can and engage in a dialogue with you on changes that will make us better. We have learned that power markets can change unpredictably and very quickly. We need to find a way to limit our exposure that is compatible with the fundamental fiduciary responsibilities of the City's elected officials. We also need to talk about hedging instruments that can protect us from market volatility. Finally, we have to continue to talk about our reliance on hydroelectric resources. I like the hydro portfolio we now manage, but it inherently has huge natural swings. There may be other approaches that could improve stability for our ratepayers, but they will come with environmental and other challenges and almost certainly with higher costs. While we have a remarkable portfolio with enviable costs and environmental performance, we must seek to make it better, more reliable and less risky.

II. Cultural, Workforce, Internal Decision Making

4. It is evident now that the decisions to not immediately and fully replace the energy supply shortfall created by the decisions in the late 1990's to sell the City's portion of the Centralia thermal plant and to rely less on BPA and more on the spot-market were critical strategic decisions for City Light. Have modifications been made to City Light's decision-making processes that have changed the way such issues will be considered in the future? What do you believe are the important lessons learned for Seattle City Light from the energy crisis of 2000-01? What has changed at City Light in response to these lessons learned?

This question is very difficult to answer because the decision not to replace BPA was driven by fundamentally different reasons from the decision not to replace Centralia. Each has its own place in the puzzle of what happened, and to evaluate the thought process around them, and whether that process needs changing, we have to understand the context for each.

The decision to reduce the BPA contract amount was made in the context of a number of very complex issues. There was a lively debate about these issues within the utility, and I believe we did a fair job of characterizing the options for the City's elected officials. In the end, Seattle arrived at a decision very similar to that of many other utilities in the region. The decision rested on the desire to reduce costs, but also to reduce the risk of customers leaving our system for lower priced power in the market.

Bonneville was more costly than the market in 1996 and the long range forecasts of the Regional Power Planning Council, the California Energy Commission and our own in-house models indicated that western wholesale market prices would remain relatively low and stable until about 2005. Over the long haul, these models generally showed that merchant generators and continued technological improvements (e.g., in combined cycle efficiency, in fuel cells, and in micro turbines) would effectively cap long term prices in the \$20-35/MWh range. We opted to take the chance on power market risk between 1996-2001 in return for a small cost cut that could help lower customer rates and reduce the chance that large customers would leave us stranded costs. By October 2001, well before 2005, we would have the opportunity to increase our reliance on BPA, should markets firm, deregulation efforts evaporate, or technological improvements stall. I should emphasize that in 1996, deregulation was seen as "inevitable." Large industrial customers and suburban jurisdictions were anxious for access to cheaper wholesale market prices. Even large commercial customers clamored for access and "choice." Our largest industrial customers and some of the suburban cities we serve were extremely active in their support for legislation in Olympia that would require us to provide wholesale market access for

retail customers. The political and analytical background was compelling. We were legitimately concerned about the potential loss of load for which we had already acquired resources. We developed a strategy to use the market to reduce our short-term rates and avoid long-term stranded costs that would inevitably fall on small residential customers.

On balance, I think the BPA contract reduction decision was well motivated, reasonably analyzed and openly debated. It turned out badly, no question about that. Would we do it again? There will always be temptations to sacrifice long-term rate stability for near-term cost cuts. We have to guard against that. Unfortunately, we may find ourselves dealing with this same problem with regard to our Bonneville contract all too soon.

Many things have changed at City Light that will serve us well in the event we face similar choices in the future. Power planning is now a process that integrates the skills and expertise of many people representing many disciplines and branches. Planning is not the bastion of an elite group with little external interaction. Our internal debates are much more balanced, less theoretical, and more mature. We have used this process to develop the current strategic resource portfolio that the City Council adopted in the fall of 2000. That portfolio broke away from the “lowest cost” mantra that had driven City Light power planning for many years. We no longer plan resources around “average water” conditions that benefit the ratepayer some years but can really sock them in bad years. We now have a power portfolio that should not leave us exposed to market purchases to meet our load in any month of the year in nearly every foreseeable water condition. That is a big change. While being surplus also exposes us to market forces, it also establishes a clear end to risk – for a seller, the floor price is zero. As a buyer during the crisis, our risk had no ceiling. We now have much greater respect for the cataclysmic risks of net exposure to a dysfunctional market.

Centralia appeared to be a reasonably priced resource in relation to likely market conditions. However, it was and still is the largest point source of sulfur and nitrous oxide emissions in the Pacific Northwest. I believe Seattle’s discussion of the Centralia decision engaged all the right players and contained extensive and excellent data. The economics of the plant were presented fairly and accurately. The City Council’s decision focused on conflicts among the owners on emissions cleanup. Seattle insisted on prompt investments in scrubbers (for sulfur dioxide control). The eight owners could not agree on the merits of that decision, nor the schedule. In the end, we could only agree that it made sense to sell the plant on the condition that the new owner install scrubbers promptly and accept all of the risks associated with cleanup of the mine. We were surprised that the plant sold with these conditions for a price above our cost, less depreciation. At that point, our only option was to support or veto the sale.

We discussed the purchase of an alternative resource to replace the Centralia power with the City's elected officials. The sale was uncertain right up to the day of closing. So, the decision to replace the power was deferred until the sale was completed. On May 22, West Coast power prices jumped to the nearly unheard of price of \$60 megawatt hour. I sent a memo to the Mayor immediately recommending the purchase of the replacement power. The purchase for the balance of 2000 was completed relatively quickly thereafter. That purchase of 75 megawatts was one of the most costly Seattle had ever made. It nearly exhausted our power budget for the year. Since the City had not adopted a budget for 2001, we did not have authority for purchases into the next year. Ultimately, the problem with budget authority and the resultant rate impacts for 2001 did get resolved with the cooperation of the City's elected officials.

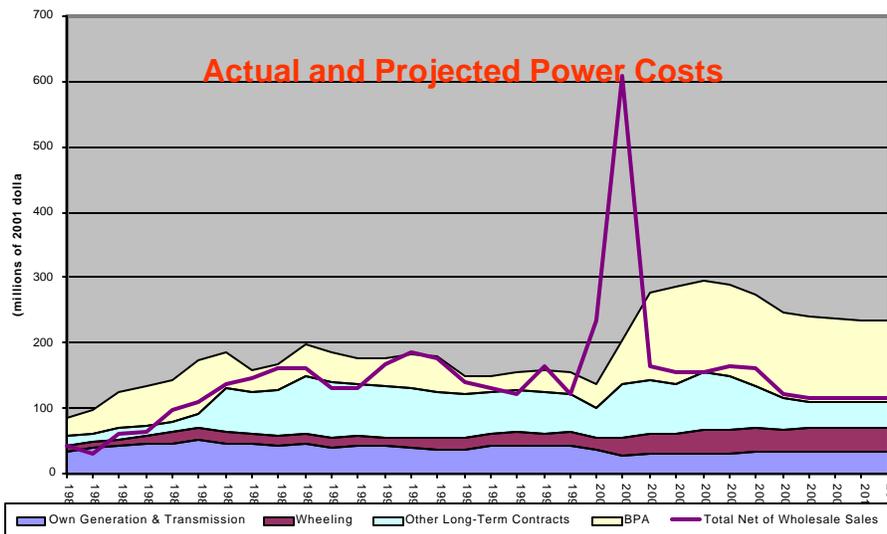
The issue of replacing Centralia remained under active consideration by the utility's risk management committee throughout 2000. The committee was split. Some argued the exposure was too great a risk and others believed it was an amount of power that could easily be handled by our existing resources in an average water year. The new strategic resource plan the City Council had adopted limited our exposure to roughly mid 2001 when the new Klamath plant and the Bonneville contract expansion would become available. With all of the weather forecasting services we use predicting normal weather for the coming winter, we postponed the decision.

It is not a decision we would make today. The new power portfolio eliminates our net market exposure in critical water—we have sufficient power supplies to meet our loads in every month of the year in virtually every reasonable water condition. We no longer plan around average water conditions. That is the most important improvement we as a City have instituted since the energy crisis. The activities of the risk management committee have become more disciplined with much better record keeping and regular reporting on the accomplishment of committee decisions. That is a further safeguard.

The risk management committee meets weekly and brings together a cross section of utility leaders whose responsibilities relate to this important part of our business. Almost every week, the committee reviews in some detail a host of changes in the forecasts for the many variables that affect the power management bottom line. I believe the debate is a good one. It has gotten even better with the addition of Executive and Council staff. In the end, we are human. With Centralia, we made a close judgment call that went badly. With the BPA decision, we made an excellent decision that was overwhelmed by later events that simply could not have been anticipated.

5. One element of corporate culture is the extent to which an organization creatively draws on all of its resources to capitalize on opportunities and address challenges. In what ways could City Light modify its existing organizational structure and internal decision-making processes to help strengthen its internal review of key strategic issues? In particular what can be done to better engage and integrate all elements of the organization in identifying strategic issues and crafting appropriate responses? Further, do you believe that the utility's current organizational structure puts an appropriate emphasis on long-range planning? For example, you noted during your original confirmation process that City Light had a well-known and widely respected process to forecast loads and plan for required resources. Does this process still exist?

I believe City Light has built on the strong planning base it was known for eight years ago and has made it much better. In our strategic business planning process, we recognized that many parts of City Light's organizational structure needed to evolve. Planning was clearly one of those areas we made much more responsive and vital. City Light currently has a more decentralized, and less model-driven process in place for long run forecasting, and strategic planning. More parts of the utility are involved, and many more legal and political issues are being considered, and weighed. The uncertainties of the industry make long term planning a part of the process rather than the end game. With the range of uncertainties, the meaning of "long term" has shrunk from the 30-year horizon used for planning 10-15 years ago to perhaps 5 years.



We also instituted the concept of scenario planning to our planning process. It is a way of visualizing various future outcomes and creating plans to succeed in those scenarios. In our business plan of 1997, we contemplated alternative futures—full retail deregulation, stalemated deregulation, and climate change—and determined that our business strategies

were reasonably strong in all scenarios. Obviously, we did not exhaust the range of scenarios that could do grave damage to the utility. We did not anticipate just how damaging a deregulation problem in California could be to our systems in the Northwest. Nor did we consider the possibility of cycles that might emphasize deregulation for several years, then re-regulation, then further deregulation. I am convinced that scenario planning is still a good model, but it does require that we

keep it a living process. We have to revisit the scenarios, evaluate the signposts, and make appropriate changes to our strategies. That committee has become more disciplined with much better record keeping and regular reporting on the accomplishment of committee decisions. That is very time consuming but well worth the effort.

We are quite convinced that the 30-year horizon built into our old forecasting and integrated resource planning models was not useful in 1996 and is not useful in 2003. Load forecasting is useful if you know that you have a clear obligation to serve within a given geographic area, and trends in usage and regulation are reasonably predictable. It is clear that we will not have state retail competition legislation in the foreseeable future, but the federal picture is less clear. Some elements of standard market design have impacts (e.g., potential stranded costs) that are similar to retail competition risks. Loads are much less predictable—the predicted server farm in 2000 -- could not have been anticipated by the most by the most sophisticated load forecasting models. Who would have guessed that regulators would refuse to intervene in such an obviously sick market? Every integrated resource planning effort I know of in the western energy market predicted large new generation plants built in the region once prices hit \$28-\$35/MWh. Most of those that were started were cancelled. The companies who started them are broke. And power costs were at \$300/MWh! There are not enough safeguards in this market to use 30-year tools.

Supply planning models are also in flux. The underlying assumptions that drive these models—wholesale prices are driven by marginal fuel costs in the short term and capped by total marginal cost over the long run—do not hold in a deregulated electric market. Over the short term, we pay close attention to all the factors that drive wholesale price—gas cost, demand growth, water conditions, and temperature. But the longer term is more opaque, and can be manipulated, as we've already seen.

I might add that our traditional long range planning models asked one major question—what's the cheapest long term way to acquire new, environmentally sound resources (conservation or generation) for carefully forecasted loads? That's a good and sophisticated question, but it is insufficient in today's world of industry changes and restructuring realities. We must integrate distribution and transmission system issues in our long term planning. We must consider end-use metering, real time pricing, distributed generation, demand-side bidding and many other factors never effectively incorporated in the long term supply planning process. I think we are making progress here, but we'll always have a ways to go.

6. The electric power industry is evolving rapidly, posing challenges that will likely force significant change at utilities such as City Light. Some have stated that City Light seems to foster a culture of defensiveness and deflection of blame when asked to look inward and consider the possibility of change. In 1994, when you were first confirmed as Superintendent, you noted that, "rather than an opportunity, change is understood as a threat to survival." At the time you committed yourself to addressing this problem. What will you do now to make City Light a more adaptable, self-learning organization that embraces rather than resists change? How will this be different than what has been done over the past eight years?

This criticism of City Light is a very difficult one for me. It is very challenging for any organization to deal effectively with as much change as we have had at City Light over the last eight years. It is also very hard for an organization that delivers such a complex and technical product that must function perfectly at every minute of every day to be other than a bit conservative about changing routines that clearly work. Being conservative and predictable about change is an absolute imperative of the electricity industry. But that does not mean that change doesn't happen. It quite clearly is happening at the utility.

The City Council, the Mayor's Office and our employees have challenged conventional utility rhetoric and practice in many areas. No organization that built and continues to operate on the the country's best conservation programs through times should be thought of as defensive. No organization that confronted conventional wisdom on deregulation should be seen as defensive. In fisheries, resource planning, human resources, the environment and other areas, City Light has had the courage to confront old ways with new approaches. Defensive organizations don't do that.

Perhaps the root of the charge is what we said at the outset of the energy crisis. We argued that there was evidence of manipulation and FERC was failing to do its job. We were criticized at the time for putting the blame on others. But I strongly believe that we were right to press FERC. Subsequent events show that there was manipulation, and getting FERC to act promptly was the only strategy that could have provided immediate relief to utilities in the West.

I think that a look at my career suggests a leader who confronts problems with candor and objectivity. No budget director survives long without encouraging candor. Many individuals who have worked for me have been selected for leadership roles in the City. I suggest that is partly because I maintain an atmosphere of learning and problem solving in the workplace.

When I originally came to the utility there were serious issues about diversity and a respectful workplace. While those issues have to be worked on constantly, I have helped create some real change in that arena. That is not accomplished with a defensive posture.

In my career, I've had a great respect for informed third party observation. The RW Beck report in 1994, for example, provided a candid look at the state of our generation infrastructure. It provided the background for the sound investments we made in the rehab of our core generation assets. I have employed the use of outside, third parties for help in framing many different issues at the utility and will continue to do that. While I disagreed with some of the conclusions of the Vantage Report, I embraced the whole of it because it pushed us to look at things anew. We are making good on the promise to address all of the recommendations of the audit and to do so quickly.

Here are five specific areas where we can do more to make certain that we are a self-learning organization:

- More and better reporting with elected officials. Candor is, in part, a product of contact, discussion, criticism and questioning. It also requires that we learn to listen carefully as we talk. An excellent example of that process at work is the development of our deregulation policy – a thoughtful, several-weeks-long discussion with the Council and the Mayor that resulted in an excellent policy background that continues to serve us well.
- Continued use of performance metrics, comparisons with other utilities, and benchmarking of key processes and activities. These can raise questions about our business practices, policies, expected levels of performance, and lead to improved levels of performance. More customer contact. We meet frequently with our key customers and carry out focus group research to help us understand what is on our customers' minds. It is always useful, and I almost always say 'I wish I did more of this.'
- The new advisory group will provide us an excellent format for another set of eyes engaged in our work and backed up by considerable technical expertise. This is a tremendous forum for the challenging of assumptions and old perspectives. Finally, we all have to do a better job of communicating with the people on the front lines, our employees. Me in particular. Our employees are the great strength of this organization. They have proven over and over again that they make us the industry leaders that I believe we are. In the press of all of the things we have to deal with in our daily calendars, we have to make more room for dialogue with our employees.

■ Finally, we all have to do a better job of communicating with the people on the front lines, our employees. Me in particular. Our employees are the great strength of this organization. They have proven over and over again that they make us the industry leaders that I believe we are. In the press of all of the things we have to deal with in our daily calendars, we have to make more room for dialogue with our employees.

Our industry is going through massive change. We need to find ways to keep us in tune with the rush of change. That means we need an environment where employees are ready to act and, sometimes, fail. Unless we have that kind of organization, too many will wait too long to do too little, and we will fail our customers.

7. In what ways do you see technological advances (such as distributed generation) changing the utility industry over the next 20 years and what is City Light doing to prepare for such changes?

As a public utility, our customers' needs and values should be the primary driver behind our use of new technology. Our customers tell us they value:

- Reliability—power that's available and deliverable when they need it. Good customer service—accurate information and efficient service from courteous, knowledgeable staff;
- Reasonable rates—a fair price for the energy they use;
- Environmental stewardship – managing our hydro resources, taking care of fish, air and water Conservation expertise – how to use electricity efficiently; and,
- Premium power – quality services for customers with critical scientific, medical or industrial processes.

With those values in mind, I'd be happy to share our current perspective on new technologies for distributed generation, central-station generation, district heating, conservation, and customer and information technologies.

Distributed Generation

I view distributed generation as a set of technologies that are installed within our existing distribution system, potentially on customer premises, that could be owned or operated by the utility or the customer. These technologies can include fuel cells, microturbines, larger gas turbines, photovoltaics, or co-generation. Distributed generation has the potential to increase our meet system loads without reliance on long-distance power transmission lines, and may offset distribution system investments otherwise needed to meet load growth. We have met with, and continue to pay attention to, advocates and analysts of distributed generation, such as Amory Lovins of the Rocky Mountain Institute. Our current assessment is that we need to stay on top of distributed generation, whether we own it or our customers own it. Our current thinking is that we will see distributed generation developed far more quickly in parts of the country where retail electric prices are in the 10-20 cent/kWh range, rather than the 4-6 cents/kWh prices in our service territory.

Solar photovoltaic (PV) systems are costly, but as more of these systems are manufactured and installed, the manufacturing cost will decrease due to economies of scale. City Light's purchase of PV systems through its Green Power program will help grow the market. We do not see cost effective opportunities – in Seattle and at this time - to rely on photovoltaics as a substitute for generation and distribution system investments.

All other distributed generation power systems currently available burn fossil fuels. These include fuel cells, microturbines, diesels, and co-generation applications. These are all serious alternatives to long term central station investments and distribution system expansion.

Fuel cells could become an attractive source of power for distributed generation. It is likely that improvements in capital cost and reliability will be driven by automotive applications now underway. We are definitely attentive to this technology, and have explored partnership arrangements with customers in this technology. To date, we have not found applications that make economic sense, but we try to keep our ears and eyes wide open. I treat this technology as an opportunity, not as a threat.

Microturbines and diesel engines may enter the market more quickly, but both have cost, reliability, and environment performance issues. Diesels can burn a variety of fuels, including bio-diesel, but they predominantly rely on distillate fuel oil – otherwise known as diesel – that may be difficult to permit within the greater Seattle air basin. Microturbines typically burn natural gas – a cleaner fuel – but lifetime, capital cost, thermal efficiency, and reliability are issues that limit general use. At some point, we expect customers with special needs (e.g., high reliability or voltage stability) to ask us to partner in the development of some distributed generation technologies. City Light will remain open to this possibility and incorporate it into staff development, business models and resource planning.

As part of our on-going strategic planning, we are analyzing the potential for distributed generation to offset central generation and distribution system investments. I have directed the Account Executive office to work with large customers and developers to assess distributed generation interest, issues and needs in our service territory and ultimately to establish a Distributed Generation Center. The account executives will draw on our technical resources in the Distribution Branch and in Energy Conservation. Our preliminary conclusions will be available for discussion in 4th quarter of 2003.

Distribution System Technologies

Metering technology is changing rapidly. New electronic “smart” meters provide customer billing data, as well as strategic information about the status of the distribution system. We are monitoring and testing these meters for potential opportunities in customer services, billing, rate design, outage reporting and restoration, peak load management and energy efficiencies.

Here are some areas in which we have already made progress:

- In 1999, we established the Power Systems Technology Unit to test and evaluate new micro-turbine, photovoltaic and distribution automation pilot technologies, along with a back-up system control center. The Unit completed a significant portion of the fiber-optic system that will link our substations and improve automation and communication at our generation facilities.
- The Power Systems Technology group is preparing a comprehensive plan for distribution automation deployment over the next 20 years, with appropriate costs and cost savings. This will be available for discussion in the 4th quarter of 2003.
- Seattle MeterWatch is providing energy consumption data to more than 100 building engineers in our largest commercial/industrial facilities. We developed new software and installed advanced meters that collect 15-minute load data. The data is downloaded every night and posted on a secure Web site. Customers include Boeing, the Fred Hutchinson Cancer Center and the Bank of America Tower. Seattle MeterWatch helps them make their buildings more efficient, saving them money and, by extension, lowering our load. This was the first time a City Department used the Internet to deliver individual customer data. We intend to further develop this service with our customers.

- In 2002, we formed a cross-divisional Meter Strategy Workgroup to study and make recommendations on how to apply new metering technology to a variety of problem areas. As a result of the group's work we recently began installing at least 300 new meters that will enable meter readers to get reads from the sidewalk for hard-to-access residences.

Changes in metering technology offer potential efficiencies and customer service benefits, but also require large investments. We need to weigh the investment against labor savings, bill production and payment efficiencies, and other potential benefits.

District Energy Systems

City Light is projecting substantial new development and load growth in the South Lake Union/Denny Triangle planning area over the next 20 years. To meet this growth traditionally would require very large investments in distribution and new new metering and communications technologies. We are now examining the feasibility of serving all or part of this load through a district energy system that is able to produce steam, hot water or chilled water at a central plant and pipe it out to buildings for space heating, water heating, and air conditioning. Individual buildings in such a district don't need their own boilers, furnaces, chillers or air conditioners.

City Light and the Washington State University Energy Program, with support from the U.S. Department of Energy, the American Public Power Association and a private contributor, are collaborating on a high-level technical and economic feasibility study of a district energy system in the South Lake Union/Denny Triangle planning area. An advisory committee will review key inputs, assumptions, and technical options and make recommendations to the study team.

An energy district offers potential benefits for customers and City Light. For the utility, it may reduce infrastructure development costs by reducing electrical demand, promoting sustainability, improving system reliability, and providing a new revenue source. For developers, buildings tied to an energy district require less capital investment because they won't need complicated individual HVAC systems, and they won't have to install backup heating and cooling systems because of the energy district's built-in redundancies. Because buildings in the district require only heat exchangers, more space is available to lease.

The Meter Strategy Workgroup is also looking at the South Lake Union area as a field research laboratory to examine new metering and related telecommunications and system automation technologies. Advances in metering and communications technology may provide efficient ways to add, read and bill the area's anticipated 10,000-15,000 new residential and commercial electric meters.

Energy Management Technologies

Seattle remains very active in assessing and implementing new technologies to improve the efficiency of electric energy use. We have participated heavily in the Northwest Energy Efficiency Alliance (NEEA), and continue to press both Bonneville and the Northwest Power Planning Council to emphasize these technologies – and continuing improvements in these technologies – for meeting incremental needs. We see continued improvement in a variety of areas, particularly those that improve the energy efficiency of commercial and industrial buildings and processes. Automated control systems, such as Direct Digital Controls, provide automated monitoring and materials control for industrial processes such as steel melting.

City Light's' commercial/industrial conservation staff work with the Lighting Design Lab to promote the latest in lighting fixtures, controls, and daylighting strategies. T-5 lighting technologies are emerging to replace "second generation" T-8 lamps in many applications.

In recognition of the rapidly changing conservation technologies, the City Light's' Commercial/ Industrial Conservation group has established a "New Technologies and Plug Load" team. Staff is designated to track, evaluate and test promising

new technologies. Also, in partnership with the Northwest Energy Efficiency Alliance, the Energy Ideas Clearinghouse is conducting product reviews on behalf of City Light and other regional utilities.

City Light and the Department of Construction and Land Use incorporate advancements in building technology into their regularly recommended changes to the City of Seattle and Washington State energy codes.

Information Technology

As customers continue to automate more aspects of their lives and businesses, they have a growing need for reliability and high-quality power, and electronic communication.

Our customers' use of technology will lead them to demand new methods of interacting with us, including electronic billing and Web-based self-service, e-

procurement systems, and enhanced interoperability of power control systems. In the near term, City Light will make investments to better integrate computer systems to serve customers, manage work processes, maintain power system assets, and manage inventory and supply chains.

Our customer billing system, CCSS, was built with interfaces to work-order management, outage management, dispatch, and geographic information systems, as well as an interactive voice response system to allow customers to access services by telephone around the clock. City Light is now redeveloping the generation and distribution work-order management systems to better support links to customer service, billing, financial, engineering analysis, computer mapping, drafting, design, and asset management systems. This increased automation will be designed to improve responsiveness to customers, make more efficient use of energy and human resources, and reduce operations and maintenance costs. Next-generation wireless communications will enable us to carry those operational efficiencies from the back office into the field.

Information technology trends are occurring against a backdrop of infrastructure and information security concerns. City Light will approach security improvements in an integrated manner to protect physical and information assets. We have subjected our initial online customer service tools to rigorous security audits and will continue to pay close attention to risk. City Light is coordinating this work with the City's Chief Information Security Officer and other departments.

8. How well positioned is City Light to cope with the coming retirement of a significant portion of its workforce? In your tenure as Superintendent, what have you done to craft and implement an effective “succession plan”? What additional steps do you recommend? What have you done and will you do to support employee input and ideas/suggestions for institutional improvements?

The average age of our utility work force is 48 years. Currently 25% of our employees are eligible for retirement, and we project that 44% will be eligible in four years. Many of these people have critical technical skills we can't always compensate competitively. We also have employees who possess knowledge about our system that simply cannot be found elsewhere. I cannot think of any more serious threat to the integrity of our business or the reliability of our service than the inability to replace these valued employees. Fortunately, I think we are keeping up with the challenge.

Several years ago, our management team started to focus on areas where we appeared to have the most vulnerability. The System Control Center, the nerve center of our system, now has recruited trained and certified a host of new dispatchers. We worked with our labor unions and agreed to a special compensation strategy that is finally helping us recruit transmission systems engineers and information technology professionals. Line workers and other trades that work directly with electricity have to learn on the job and our expanded apprentice programs and facilities are industry leaders. While we think we have good people ready for promotions in many critical areas, there are too many gaps.

I have made it the responsibility of each member of the Executive Team (Deputy Superintendents and Directors who report to me) to assess their future workforce needs and implement plans to replace key positions. We have taken several steps to establish a succession plan to identify, develop and replace the key positions we will need to deliver essential utility services in the future.

Accomplishments to date include:

- Baseline reports on City Light employee retirement eligibility now and projected through the next four years, average employee age data, and utility attrition (turnover) data. (The City of Seattle is using City Light's data model in creating similar reports.)
- A survey of other utilities' and governmental organizations' succession plans;

- Continued development of the utility's Apprenticeship Program, which includes seven different programs for training skilled-trades employees and maintenance laborers to become qualified journey workers; and,

- Development of an all-employee training database to track required licenses and certifications. The database also establishes a record of the training provided to each employee through our training plan.

Several other activities are currently in progress to address the workforce issue. A management survey now under way will identify key positions and skills needed in the future. We will also perform an assessment of current workforce skills and measure that against skills needed in the future to identify "gaps."

Our ability to effectively develop and support diversity will help us meet our workforce needs. Our supervisor/management training project is designed to provide all supervisors with the tools they need to develop and effectively manage a quality diverse workforce.

Recognizing that we don't operate in a vacuum, we have begun an analysis of industry and workforce trends that could affect our succession planning. There are some very interesting ideas we can capitalize upon, as this is clearly a concern that many other utilities are currently struggling with.

As we make progress on the initiatives currently before us, we will collaborate with our labor unions and with City Personnel and other departments on broader, citywide succession planning activities.

Our future is at stake. This will be a very high priority for the men and women of Seattle City Light.

9. What have you done and will you do to support employee input and ideas/suggestions for institutional improvements?

City Light has a number of formal employee communications programs that serve us reasonably well, but what is really important is that we have a culture that makes it clear that we really value our employees' ideas and contributions. We can always do more in this regard and we will. I get around the utility with some regularity just to talk informally with employees. Employees make good and frequent use of my "open door" policy and they certainly know my e-mail address and phone number. If there is one thing that seems to me to be absolutely true about City Light's culture, it is there appears to be very little bashfulness about telling the boss what is on someone's mind. People don't always get the answer they had hoped for, but they do get an attentive listener and an honest response. The interaction with employees is one of the things that sustains me in this job. I know I need to make more room on my calendar for this.

In periods of incredible change, it is very important to share information about external events broadly. City Light has a number of publications that keep our employees informed. Our internal and external web sites are getting good use as a communications tools. We also put out a daily "News You Can Use" e-mail that captures news about the electricity industry from around the country. We have a regular lunch time speaker program that encourages our employees to interact with internal and external leaders of key projects or issues City Light is engaged in. Our monthly employee newsletter, Network, features employee accomplishments as well as important information about the utility.

Since 1984, City Light's Light Power and Pride program has offered our employees the opportunity to recognize the exceptional achievements of their co-workers. Our recognition program provides a visible, powerful way to communicate and reinforce successful behavior, encourage and support the achievements of collaborative work groups and teams, and reward creativity, innovation and initiative.

City Light's Leadership Forum – which includes the utility's entire management staff, from supervisor to superintendent – meets quarterly to discuss utility issues and develop City Light's new business plan. Between quarters, smaller work groups meet to discuss planning scenarios, which they bring back to the larger group. This group provides critical feedback on current issues and is essential to shaping the direction of the utility.

Each year I talk about the state of the utility with employees at each of City Light's far-flung facilities. This is another opportunity for me to meet employees face-to-face, provide a comprehensive assessment of the year's events and respond to their questions and concerns. It is a lively and valuable give-and-take

with employees not known for their reticence. It puts me in touch with workplace issues at our different facilities and gives employees a framework for understanding the broader issues the utility is facing.

“Ask Gary” is a new feature being developed for City Light’s internal web site. Employees will submit questions, comments or suggestions about the utility directly to me, and I will respond. The “Ask Gary” web page is scheduled to debut by the middle of March.

City Light’s joint labor management committees meet bimonthly to discuss and resolve issues facing City Light management and its many labor unions. These are very lively meetings. The dialogue is strong but so is the product. We resolve a host of problems in these forums. I attend frequently and the utility always commits top management to JLMC work.

10. Compare City Light's workforce profile with EEO availability rates for women and minorities during your tenure as Superintendent. How can you make the utility more inclusive?

More than ever, City Light's workforce reflects the diversity of the community it serves. More important than just meeting the numbers, there has been a dramatic change in the City Light culture. It is a change that might have been overdue eight years ago, but I think it is absolutely clear today that our employees are now proud of their diverse and respectful workplace.

The utility's EEO profile at year-end 1995 showed that the make-up of our workforce did not reflect EEO availability rates in three overall categories for minorities. There were five EEO categories for women where the composition of the utility workforce did not meet the availability rates.

As of year-end 2002, our EEO profile shows that the utility's workforce now meets, or exceeds, the EEO availability rates for total minorities in every EEO category. For women, the make-up of our workforce is lower than the EEO availability rates in four categories. Those are Technicians, Para-Professionals, Office & Clerical, and Service & Maintenance.

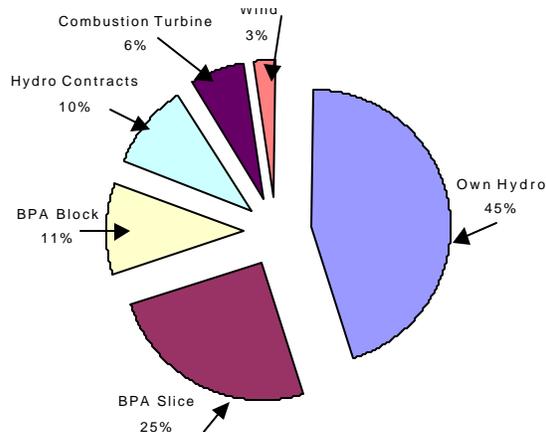
I am proud of our commitment to a diverse workforce, and constantly look for ways to make the utility more inclusive:

- Recruitment, retention, development, mobility:
- Institutional barriers to inclusiveness such as employment processes, promotion strategies, temporary assignments;
- Department-wide training on EEO and Americans with Disabilities Act;
- Employee input and identify issues, barriers, and opportunities in the workplace; and,
- Partnerships with employee, professional, and community organizations, notification of employment opportunities at the utility, and active presence in their activities (Women in Science and Engineering, MESA Internships, CLBEA, FACES, Women in Trades, NAACP, Urban League, Minority Executive Directors, vocational schools and universities, etc.)
- City Light's Black Employees Association (CLBEA) is a group we are all proud of. They are real leaders for black employees not just in City Light but throughout the City. I meet regularly with their leadership. They will continue to have my ear and my support.

11. In your response to the Vantage Report, you acknowledged the need for City Light to “do a much better job of tying our analytical skills to our strategic objectives, tactical plans and our discussions with the Mayor and City Council.” How will you do this? How will you infuse risk management considerations into major utility decisions beyond power marketing ones?

We must get on with the strategic business planning process. This is a great opportunity to get the Mayor, Council, customers and the utility on the same strategic path. That’s job one in the alignment of our analysis with our plans.

We are in a different position now than when we did our last business plan in 1996. While we thought we were in a very volatile time then, there is no comparison to today’s volatility. Today’s times mean we must be able to act quickly and that requires agreement on the broad strategy. It requires that it be a living document, changing as circumstances change and a part of all our discussions. The business plan sets the overall direction and tone for a host of other planning activities that we routinely engage in, but three deserve particular mention here: resource planning, financial planning, and capital improvements planning, particularly for our distribution system.



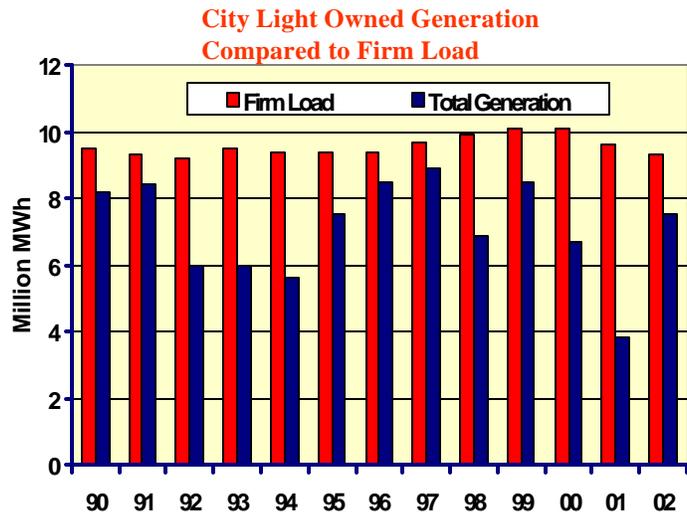
Although we now have a portfolio that will cover our customers’ needs in low water conditions for the rest of this decade, we face some issues that will need policy level guidance. While our portfolio is very competitive, it does give us a unique risk profile that must inform financial policies as well as future resource decisions we face around the Klamath Falls Combustion Turbine and choices we need to make about BPA.

As part of the Strategic Resources Plan Update, we shared with you a modeling framework that encourages consideration of the financial risks associated with different resource decisions.

Changes being pushed by FERC could dramatically alter the value of our generating resources, and we need to stay on top of that both from the policy and planning perspectives. We have a lot of work yet to do to understand the implications of these changes for City Light, and as that work gets done we will seek policy guidance using the business plan as our guide.

We have already addressed new financial policies with our elected officials, and we believe the new policies provide sufficient depth to manage our current challenges. However, as we learned in the past, we need to be forward-looking and to anticipate new challenges. Relationships between water conditions and electricity prices and between electricity prices and broader energy prices are constantly changing and affect the probabilities of financial outcomes.

And there are other risks: interest rates are at historical lows right now and we are benefiting from them, especially in the short-term debt market, but we cannot expect rates to remain low forever. The same could be said for inflation. We must use the process to identify all the business risks we face, and be prepared to deal with them.



We also need to consider the role of debt in our major capital improvement projects. City Light has assets under its care worth billions of dollars. These assets need prudent re-investment to ensure that future generations can continue to enjoy their benefits.

As I noted elsewhere, while we have largely completed a much-needed rehabilitation of our generation plant, we are only just beginning a major planning effort around our distribution system. Like the generation overhaul, this will be a long and expensive process. Planning will be especially challenging because of the possibility of significant regulatory and technological change during the execution of the plan. Understanding the differing pressures affecting our power supply and power delivery lines of business will be very important. We need to have a process that is flexible enough to address major changes in the business environment in which we sell retail energy.

We will engage the help of a top-notch consultant to help us think through many of these issues. That approach worked very well in the past with the generation rehabilitation, and I am confident that it will work well again.

As we move into the future, we will have many opportunities to engage our elected officials: the business plan, rates and budget process, CIP program review, accountability, and financial updates, to name just a few. These are all critical matters for the utility. We are looking forward to working with the City's elected officials as you engage in these important policy decisions.

III. Relations with the Council and the Public

12. The Council relies on City Light to provide data and analysis to the Council in a timely way in order to make appropriately informed decisions. In recent years, Councilmembers have expressed concern with receiving timely information with all options presented in response to our questions and on occasion, it appeared as though information provided was primarily intended to support the Executive's recommendation, compromising informed policy decision making and trust between the Council and the utility. Can you suggest ways that you as Superintendent could work with the Council to expand the breadth and timeliness of information we receive from the utility? How will you communicate with Council when there is a difference of opinion between the Executive and the Council? At the time you were originally confirmed you committed yourself to "communicating effectively" with Council and being genuinely supportive of City Council's policy role. What will you do over the next four years to improve communication? More generally, what do you see as the utility's responsibilities with regard to the type (depth, specificity, range, etc.) and timing of information provided to the Council?

The commitment I made at my initial confirmation to communicate effectively with Council is one that I hold to. I believe now, as I did then, that open and honest communication between any City department and the Legislative Branch is critical to good government.

Keeping clear lines of communication open between the Executive and Legislative branches can be difficult, and I am sure that we had not always done so. But let me reassure you, that whatever the result of our efforts, our intent has always been to staff the Council fully and honestly so that it can provide us with well-informed policy guidance. And let me further assure you that I will do all in my power to honor the commitment I made.

Some things will help as we go forward. For a start, knowing there is a problem is clearly the first step in addressing it. We may not fully understand yet why our staffing has not hit the target in the past, but with clear feedback from our elected officials, I am confident that we can address any shortcomings. I am very supportive of the agreement the Mayor's Office and City Council members reached recently to jointly explore the communications issues that involve us all. I am confident we can come up with a protocol that will help us identify the issues and establish expectations to get us off on a more successful direction.

The fact the Mayor and Council are increasing the amount of staff time available for energy issues will create better alternatives, more critical questions, and lead to better analysis of City Light proposal.

The Advisory Panel should help in communication. It may ask different questions and come at issues differently from either the utility or the Council, and that will challenge us to broaden our thinking.

I think a more structured approach to both our work program and policy direction will be helpful, and we have already begun that process. Concurring resolutions on the work program will help me allocate our already stretched resources to the issues that really matter to elected officials. And adopting policy by resolution will provide sharper direction to the utility.

The efforts around our business planning process will also help our communication. When we agree on a final plan, the utility, the Mayor, and the Council, will have a shared sense of our strategic direction.

13. *What will you do to ensure adequate stakeholder input bearing on major City Light decisions, encouraging input from a broad range of interests? What ideas do you have to increase public confidence, stakeholder participation and to provide the public with sufficient information in a timely manner to facilitate critical, well-informed evaluation of City Light's options, proposals and supporting analysis?*

We have an excellent opportunity coming up this spring when we embark on our Strategic Business Plan outreach. We will employ a number of different techniques to find out what is on the minds of our customers. This will include small group discussions with our key customer group who are mainly knowledgeable about energy markets and from the commercial and industrial sectors. We will meet with small business associations and neighborhood business groups in a series of meetings that bring them the ranges of options we have under consideration and the consequences of those options. We will hold discussions with neighborhood and service groups to gain perspectives of our residential customers. The efforts around our business planning process will also help our communication. When we agree on a final plan, the utility, the Mayor, and the Council, will have a shared sense of our strategic direction.

We can also conduct research – focus groups, polling – that we can use for our own purposes internally as well as for a base of discussion with our customers.

Another idea that has served Seattle City Light well in the past is to convene a series of technical workshops. Many of our stakeholders are highly conversant with the issues and can offer good advice. These can be good forums to bring in outside experts who can broaden our thinking on emerging issues.

We also want to integrate the new City Light Advisory Board into this conversation about outreach. That group needs to be an active participant in the strategic business planning process, but they may have good ideas about how to engage the general public and key stakeholders in the process.

We should begin our process with a good review of what other utilities in the region and around the country have been doing. Several Northwest utilities are completing planning processes now and may have some good ideas about effective outreach approaches.

Once we have put together a draft plan, we can take that to our community through meetings, direct mail, municipal television, the Internet, our speaker's bureau.

In a broader sense, I'm a strong believer in seeking out customers and providing real opportunities for meaningful dialogue. Merely calling a meeting is not sufficient. We have fairly robust regular communication with customers when they sign up as a customer, when we send them a bill, when they call with a complaint or question. Thousands of customers each month visit our web site. We regularly speak to community groups. Combining all of our regular dialogue with customers to special communications on particular themes can create quite a lot of attention for a key idea or proposal.

The internet is, of course, a fantastic tool for communicating with all customers. There is enough information for the most dedicated energy junkie to someone pursuing a small piece of information. Combining the qualities of the internet with our regular information is something I'd like to do more of. We can do this, while still being sensitive to those who lack or have limited access to the internet.

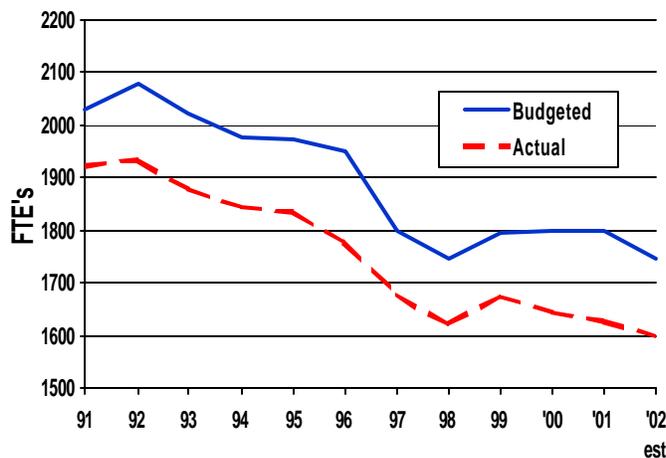
IV. Financial, Infrastructure

14. The Vantage Report suggests that there is room for City Light to trim its O&M budget further and perhaps reduce staffing levels. Do you agree? If so, how will you begin the process of reducing the O&M budget? If not, do you believe the current level of expenditures is optimum?

I do not agree with the report in this instance. It was simply a statement with no supporting information. However, I am committed to analyzing our O&M needs and performance and comparing it to our industry peers. Once I've done that and have data to support a conclusion, I'll come to one.

As a public power utility, we have an obligation to assure that we are always spending our money in a manner that keeps service levels and reliability high at the lowest long term cost. We take this seriously and look forward to reviewing our costs with executive and legislative staff. But we are not strangers to active cost management. Over the last several years, keeping pressure on costs has yielded some good results.

Budgeted vs Actual Positions



For example, Vantage pointed out that our rate of non-power O&M cost growth was below inflation and customer growth between 1991 and 2001. Their figures show our O&M increased at 1.2% per year, about a third of 3.3% combined rate of growth of customers and inflation. The annual savings from the slower growth rate was \$23 million in 2001 alone, while the total savings over the 10 years exceeds \$120 million.

We have reduced actual staffing levels by 291 FTE's (15%). Nearly 75% (216 FTE's) of the reduction has occurred since I became superintendent.

I have a good track record of managing and controlling costs. Over the years I have learned that the critical factors for success in the long run are clear purpose, connection to the business strategy, and individual commitment across the department.

When I first came to City Light, the Department was struggling with making budget reductions to meet savings commitments assumed in the adopted rates. In

addition, the City Council had set a position cap and an expectation for staffing reductions that were to be accomplished. The result was that the very people we needed to help us identify savings to meet the financial goal were too fearful about their own personal security to constructively participate. Freeing them of that fear became the key to unlocking the budget savings we ultimately achieved. The original goal of the rates forecast back then was to save ten million dollars in four years. We accomplished that in less than two. Focussing on dollars rather than staffing levels or positions also reinforced our commitment to real cost savings rather than body count, providing a reinforced sense of security for our work force. Ultimately, we also reduced a significant number of positions, and managed to avoid layoffs until this last summer. Now, as we're currently staffed at about 1625 FTE's, it seems ridiculous that there ever was such concern over a position cap of 1973 FTE's

The subject of optimizing O&M levels needs more thoughtful evaluation in order to properly answer this question. The overriding focus on rates in the past resulted in lower rates in the short term and higher debt for our utility. Those practices, once considered prudent for keeping rates low are now being criticized. While our new financial policies will help reverse the recent financial trends, we will also strive to optimize our resources by striking the most efficient balance of Capital and O&M. To do this we are proceeding with the following programs:

- Develop work management to capture and control the critical and priority maintenance work (pilot in place in Generation and expanding into Distribution);
- Improve capital project justification and prioritization (in place in Generation and expanding to Distribution); and,
- Evaluate the use of large load connection fees to reduce the impact on existing customers for significant expenditures for growth in the system.

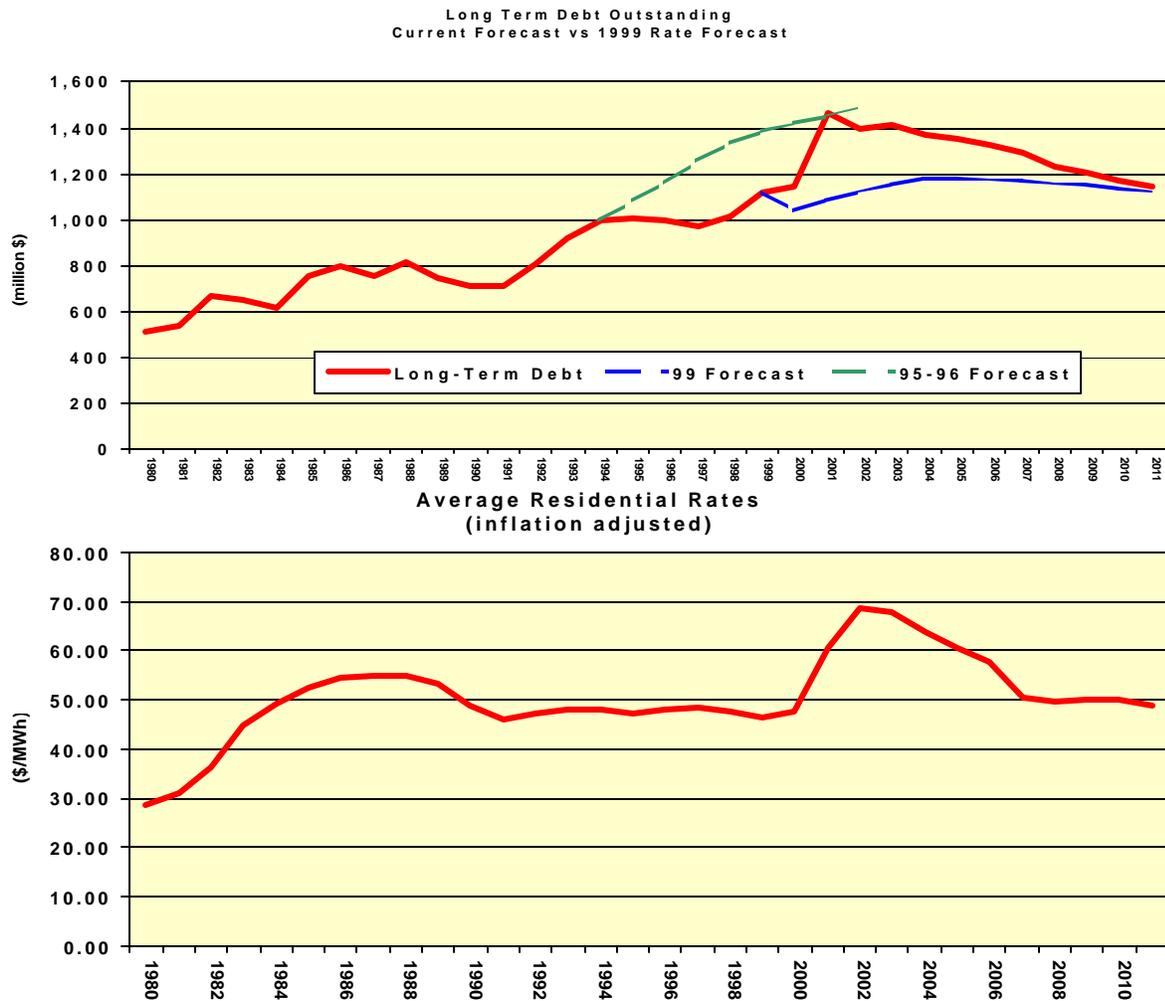
I'm a big believer that we should learn from what others are doing. We are updating the utility cost comparisons we did a few years ago. We are currently producing a detailed analysis of our general and administrative costs, and investigating benchmarking studies dealing with Distribution and Customer Accounts.

There is always room to improve the oversight of our spending and ensure that we are maintaining the value of our utility for our future. The programs that we are putting in place have already shown that we can contain the cost of production while maintaining the reliability of our equipment.

I believe our primary goal is to deliver low cost reliable service to our customers. Managing costs is just one element of that. I will always be looking for ways to improve efficiency and reduce costs while meeting our customers' expectations for reliable service. I will not risk service quality to achieve an arbitrary budget savings target.

15. City Light's outstanding debt has increased significantly in recent years. Some observers have characterized City Light as now overburdened with debt. During your original confirmation process you noted that, "debt is increasing to pay for badly needed capital investments, but rates are about to become very stable, and if we continue with current policies, our debt to equity ratio should return quickly to strong historical levels." Why hasn't this prediction come to pass over the last eight years? How would you characterize a prudent debt burden for City Light and what, if any, changes in policy or practice at the utility do you recommend to get to and maintain a sustainable level of debt?

When I became superintendent in 1994, the department was just coming off two years' of drought that had required the imposition of drought surcharges on the rates. The Council was just finishing up its rate process for 1995-1996.



The financial forecast underlying the 1995-96 rates projected that by 2000, Debt would increase 72 %, from about \$800 million to nearly \$1.4 billion, and average system rates would also increase 29% from \$37.54 to \$48.42.

By 2002, debt outstanding was to have exceeded 1.5 billion, and average rates were to have reached \$53.59, and our debt to capitalization percentage was to increase from about 70% to 75%.

These projections at the time, seemed out of synch with an industry focussed on deregulation and competition. We committed ourselves to taking action to reduce the rates of growth in both debt and rates. Indeed, in 1999, when we set base rates for 2000-2002, our projections had rates growing at less than half the rate of inflation to \$41.59 and the growth in debt outstanding was cut in half. The debt to total capitalization ratio remained stable at 70%.

What happened? By far, the largest single event was the energy crisis and the drought of 2001. All our achievements over the preceding six years in debt and rate reduction went out the window at least temporarily. Rates and debt both increased dramatically as we executed a balanced approach to this unique situation. To ensure long-term stability, we built a resource portfolio that meets load even under drought conditions, and recommended changes to our financial policies to stabilize rates and debt levels in the future. We are largely on track in our recovery plan and look forward to fully implementing our new financial policies during 2004.

The new financial policies provide a good foundation for prudent levels of debt and rates in the future. I don't believe it is accurate to characterize our outstanding debt in alarming terms. We have provided the City Council with good information that shows our debt levels are comfortably around the average for comparable utilities. That isn't to say that our current levels of debt may be higher than we would prefer. I tend to think they may be, but that is ultimately an issue we need to discuss further with the policy makers.

There are some things we should do to assure ourselves of the prudence of the track we are on. First, we should set for ourselves a bond rating target. It is interesting that the quality of bond ratings isn't necessarily correlated with the amount of debt outstanding, but such a goal would be useful in reinforcing the need to monitor what others are doing to maintain credit quality. Second, it is important to relate the debt/rate choices back to our two lines of business, which may face much different business pressures in the future. Finally, there are fundamental tradeoffs between the level of debt and the level of rates we charge our customers. Our work on the business plan and the financial strategies that will accompany it must focus on these tradeoffs and describe the full range of choices we can make.

16. When difficulties emerged with City Light's billing system early this year, some felt that City Light was slow to respond to customer complaints and then responded defensively to public inquiries about the issue. What is your reaction to this perception? What circumstances are responsible for inaccurate billing and what steps do you propose be taken to prioritize accurate billing for customers?

In April of 2002, media stories began to focus on billing issues at City Light and to highlight particular customers who received "high bills". While I can understand the perception that Seattle City Light may have been slow or defensive, let me assure you that was not our approach or intent. City Light staff immediately began to analyze the billing issues that were presented and to assess the adequacy of the billing system. I can understand how the time interval spent researching the causes of potential billing problems could have been perceived as slowness to respond. We felt a necessity to do due diligence on a system that produces approximately 10,000-12,000 bills per day.

During this time, Mayor Nickels mandated that the utility address customer complaints within two weeks and in the customer's favor if the complaint was not dealt with in that timeframe. In addition, I provided staff with my philosophy on customer service:

- The customer is important, and we need to own his/her problem;
- Problems should be handled promptly and courteously and to the customer's satisfaction;
- Fix the problem simply and permanently.

On October 1, 2002, we presented to the Mayor, City Council and the public a report entitled "Strengthening Customer Service at Seattle City Light" which detailed the range of problems we experienced and our plan for addressing them. I highlight below the steps we took during the discovery process last spring:

- The computer billing system was audited by IBM to confirm that it performed the calculation of bills properly;
- Bills created on January 31 and February 1 of 2002, a period of time when the billing parameters were slightly altered, were re-reviewed to determine if a bill adjustment was appropriate;
- Additional temporary staff was authorized to provide a more thorough check of bills before being sent to customers;
- Credit and collection activities were held while we ensured that customers working with us or in active dispute were not disconnected; and
- Focus was increased on auditing data entered into the computer system.

These steps took time to fully comprehend the reason why anomalies occurred and how they could be fixed permanently and, more importantly, prevented.

Providing City Light's 356,000 customers with timely and accurate bills is an extremely high priority for City Light. To accomplish this, a multi-pronged approach has been used which includes the following activities:

- Business processes are being reviewed so that work is streamlined, adapts to the CCSS requirements, and is performed uniformly utility-wide. Some stunning successes have been achieved, resulting in dramatically lower error rates, excellent hand-offs between work groups and ensuring accurate and timely bills.
- Backlogs, which developed in nearly all work areas after the computer conversion in April of 2001, have been virtually eliminated in three key areas of high volume work: meter installs, removals and exchanges; applications for electric service (RESAs); and meter reading exceptions (the human review that occurs before a bill is sent to increase accuracy of billing). The last remaining backlog is for billing adjustments, and we have set a goal to eliminate it by March 31, 2003. Progress on getting and staying current is monitored each week through a series of performance metrics. The City Council authorized 13 new positions for these high volume areas of work, and hiring processes are underway. These permanent positions will replace temporaries that were authorized in the spring of last year.
- We are auditing our bills for quality assurance through additional means beyond the rigorous pre-bill audit function inherent in the new CCSS. These steps help us to catch problems and resolve them before a bill is sent. In addition, the Council approved our request for an auditor position to assist the department with utility-wide protocols to increase quality assurance. This position will be filled in the first quarter of 2003.
- We have purchased and are installing meters that can be read via radio frequency. This allows meter readers to read hard-to-access meters remotely, that is, outside a locked building or gate, thus ensuring an actual read for billing purposes. Actual remote reading will occur early in the second quarter of 2003.
- We have been actively working with the CCSS vendor, SCT, to incorporate key improvements that will be included in the next software upgrade, likely occurring in late 2004. Interim solutions are being devised for the most urgent matters, requiring additional business process refinements and manual solutions.
- A focused series of customer service training started in November and will be completed in March. These were designed to assist employees at all levels to learn or get refreshed on tools and practices for customer service relationship building, problem solving, and reinforcing the importance and value of internal customer service. Workplace expectations relating to training outcomes are being reflected in individual employee's performance evaluations, and additional training needs are being identified to build on the foundation that has been established.

These steps are intended to strengthen City Light's ability to produce accurate and timely bills and to reinforce the customer service ethic that is the hallmark of public power.

17. City Light is understandably under great pressure to cut costs and stabilize rates. As Superintendent how will you work with the Council and stakeholders to balance the need not to defer CIP that could either compromise quality of service through deterioration of assets or cost ratepayers far more in the future with the need to provide affordable power now? What additional steps are you committed to implementing to ensure that CIP dollars are spent wisely?

During my tenure as Superintendent, we have rebuilt or replaced much our basic infrastructure including powerhouses, the system control center, service centers, and even our financial and billing systems. In recent years, we have struck a decent balance between the need to adequately refurbish our capital plant with the need to conserve our capital resources. Our work with the generation side of the business is reaching the conclusion of the start we began in 1996, but we are looking at potential issues on the distribution side.

At the time I became Superintendent at SCL, the utility was notorious for 1) overestimating the annual funding necessary to support its CIP program, and 2) making little progress on some individual projects while grossly overspending on those projects within the CIP where progress was made. The Boundary Rehabilitation Program was just starting on the heels of a rather poorly managed and woefully overspent Diablo Rehabilitation Program. The Council was rightfully concerned, and with its support, I directed the Generation Branch to adopt a rigorous process in addressing and funding its capital improvement program. This process has been extremely successful.

The Boundary Rehabilitation Project is now starting to wind down, ahead of schedule and under budget. For the past several years, the CIP performance of the Generation Branch in general demonstrates that the necessary work is getting done on schedule and within budget, without huge excesses of budget left over that would be indicative of unreasonably high budget contingencies. Furthermore, there is a steady trend of reduction in both CIP budget authority requests and actual expenditures. CIP funds are being well-spent on the work that really needs to be done. We have already extended the capital oversight process used for the Boundary Rehabilitation Program to all of the Generation Branch capital expenditures and is now being implemented in other Divisions. Projects are regularly reviewed to assure that the scope of work and expenditures are in compliance with the annual plan and meet the project's objectives.

In order to support moving these improvements into the rest of the Department we must:

- Do the preliminary assessments and planning necessary to identify problems/issues needing attention;
- Develop a menu of optional solutions;
- Review and modify the economic evaluation model to support more areas of investment;
- Expand the project management model and train project managers in the process;
- Build financial reporting systems that assist project managers in tracking costs in a timely fashion;
- Improve project management tools to support job estimating and reporting of construction progress.

By adopting similar approaches across the Department in developing the CIP, we hope to capture the kinds of benefits we realized in the Boundary Rehabilitation program in the broader capital improvement program. Bringing on some outside expertise to help us with the planning of our distribution system capacity needs will be a good start on this major challenge, and provide a great opportunity for us to work together. I am confident that with this disciplined process, we will be able to effectively meet our critical CIP needs for the next several years within our financial constraints.