MINUTES OF JOINT CITY COUNCIL AND LES STAFF PRESESSION MEETING
LINCOLN CITY COUNCIL
MONDAY, AUGUST 4, 2008
COUNTY-CITY BUILDING
555 SOUTH 10TH STREET
LINCOLN, NEBRASKA 68508

CITY COUNCIL MEMBERS PRESENT:	Robin Eschliman, Dan Marvin, Ken Svoboda, John Spatz, Doug Emery, Jon Camp
CITY COUNCIL MEMBERS ABSENT:	Jonathan Cook
LES STAFF & COUNSEL PRESENT:	Terry Bundy, Todd Hall, Shelley Sahling-Zart
OTHERS PRESENT:	John Hendry, Trish Owen, Craig Ediger
MEDIA PRESENT:	Jill Johnson – KLKN-TV, Karina Kling – KOLN/KGIN-TV

Council Chair Robin Eschliman welcomed Lincoln Electric System (LES) to the City Council pre-session meeting at approximately 10:00 a.m. LES Administrator and CEO, Terry Bundy, introduced LES staff and proceeded to provide an overview of a proposed increase in electric rates.

Bundy reviewed the need for LES to seek an increase in electric rates. (Exhibit I) He noted that LES has seen significant volatility in natural gas and wholesale electricity market prices. He noted that prices for electricity in the wholesale market tend to follow the price of natural gas as utilities with excess coal generation capacity will sell that capacity into the market at prices that are just slightly more competitive than the price of natural gas generation. Bundy noted that LES has a hedging strategy for natural gas purchases that has mitigated some of the volatility. He noted that LES normally hedges, or forward contracts, for about 65% - 70% of its natural gas needs and purchases the remaining 30% on the spot market. Spot market prices have averaged about 45% greater than what LES had forecast in the 2008 budget. Councilman Svoboda noted that natural gas prices have declined recently and asked about the impact on LES. Bundy responded that the lower natural gas prices would help LES, but he also noted that LES has not yet seen a corresponding downward shift in wholesale market prices for electricity.

He also noted that this volatility in energy prices is not unique to LES. He noted that LES is seeing an increasing number of utilities across the country announcing rate increases. Council Chair Eschliman asked what kinds of increases are being announced by other Nebraska utilities. Bundy responded that he is not aware of any recent announcements from other Nebraska utilities, but they may have tools to deal with the price volatility that LES does not have. For example, other utilities may have higher levels in their rate stabilization funds that give them some flexibility to absorb higher power costs. He noted that recent news indicates that Omaha Public Power District (OPPD) will see a

65 percent increase beginning in 2009 in their costs to transport coal to their power plants. It was reported that this will add $90 million to OPPD's budget in 2009. Bundy noted that while OPPD has not announced any rate changes, it is likely that these additional costs will result in rate changes for OPPD.

Bundy explained that internal natural gas resources and purchases in the wholesale electricity market together account for about 9.5% of LES' energy mix. He noted that prior to the addition of the Walter Scott, Jr. Energy Center Unit 4 coal-fired plant in Council Bluffs, natural gas resources and purchases accounted for about 25% of LES' energy mix. The addition of the Walter Scott Unit 4 has significantly reduced LES' reliance on natural gas and the wholesale market. He went on to note that although natural gas resources and purchases are only 9% of the energy mix, they account for about 31% of LES' total power costs. He also noted that these costs are running on average about 45% higher than forecast in the 2008 budget.

He went on to explain that LES' interest income is also expected to be reduced by about $3 million due to lower interest rates and lower fund balances. Current projections indicate that LES will incur a financial shortfall of about $9.3 million by the end of this year due to significantly higher power costs and lower interest income. Bundy noted that if the entire shortfall was recovered through rates, it would require a rate increase of 14.1%.

Bundy reported that the LES Administrative Board Budget and Rates Committee began meeting in late June to address the anticipated shortfall. The Committee initially looked at making $500,000 in internal cost reductions and using $1 million from the rate stabilization fund. The remaining shortfall of $7.7 million would have required a rate increase of 11.8% The Committee continued to refine a proposal and Bundy indicated that he asked LES Vice Presidents to conduct a thorough review of budgets to identify additional cost reductions for 2008. Staff identified cost reductions totaling $1.1 million and the Committee recommended using a total of $1.5 million in rate stabilization funds to bring the proposal for a rate increase to 10.1 percent. The LES Administrative Board decided at the July Board meeting to move this proposal forward for public input. Bundy noted that LES has a public meeting on this proposal scheduled for Tuesday, August 5, 2008, at 7:00 p.m. The LES Administrative Board is scheduled to make a final recommendation at its August Board meeting on Friday, August 8, 2008.

There was discussion regarding the rate stabilization fund. Bundy noted that the fund balance at the beginning of 2008 was about $2.4 million. The 2008 LES budget includes making a $2 million contribution into the fund which would bring the 2008 year-end balance to about $4.4 million. Based on the current rate proposal from the LES Administrative Board to use $1.5 million from the fund, the projected year-end balance would be about $2.9 million. Bundy indicated his reluctance to draw the fund down any lower because there needs to be some remaining cushion to deal with other unexpected contingencies that could occur, such as loss of a major generating unit. He noted that LES is planning

to budget about $2 million a year to be added to the fund until the fund balance is somewhere above about $12 million. He noted that the rating agencies would like to see the balance around $12 million or higher.

Councilman Camp asked for additional explanation of the internal cost reductions for 2008. (Exhibit II) Todd Hall explained that about $130,000 of the reductions are in labor costs for 2008. He noted that these are hiring decisions that are being deferred to 2009 and that they do not involve decisions that will impact safety or system reliability. Hall then noted that travel and training costs are being reduced by about $250,000. This includes things like IT support seminars, business seminars, and training courses. He also noted that purchases and services are being reduced in the amount of about $720,000. This includes items such as consulting services, software package purchases and upgrades, cancellation of remaining advertising for 2008, deferral of facilities maintenance and improvement, and deferral of inspections at the combustion turbines.

Council Chair Eschliman asked about LES' development of a sustainable energy program. She noted that when LES discussed it as part of the 2008 budget, there were concerns that LES did not have enough details in the program. She asked if progress had been made in developing the details. Bundy noted that staff has been working on developing the program in greater detail and that LES will be presenting those details in the 2009 budget which will come to the Council later this fall. He also noted that LES is looking into participating in some of the wind projects that have recently been announced by Nebraska Public Power District. Councilman Marvin asked what market rate LES expects to pay for wind from those projects. Bundy responded that he expects the price to be in the range of five to six cents per kilowatt-hour. He also noted that LES would receive renewable energy credits which can be sold.

Bundy concluded by indicating that LES lacks the tools that some other utilities have to hold off or mitigate these kinds of rate increases. Tools typically used by utilities include higher levels of debt service coverage, higher balances in rate stabilization funds, and power cost adjustments. He noted that LES' debt service coverage is very low compared to other AA rated utilities, many of which have debt service coverage above 2.0. He noted several comments from the rating agencies in their most recent ratings for LES, some of which note the Council's responsiveness in approving rate adjustments to meet LES' needs. Bundy expressed appreciation to the Council in understanding LES' needs and responding accordingly in the past.

Finally, Bundy noted that LES is still projecting the need for an additional rate increase in 2009, probably in the March timeframe. Based on the current rate proposal, LES is estimating a 2009 rate increase in the range of 1% - 4%. Bundy noted that if additional rate stabilization funds are used to lower this rate increase, it will mean that the 2009 rate increase will need to be higher. He also noted that LES' most recent report to the rating agencies indicated a plan to have $6 million in the rate stabilization fund by the end of 2009.

Councilman Spatz asked if there are programs for low income customers to help them deal with rising energy bills. Todd Hall indicated that Lincoln Action Program (LAP) has a Residential Energy Assistance Challenge (REACH) program that offers payment assistance and energy efficiency workshops for low income individuals and families. He also noted that LAP administers the LES Energy Assistance Program that provides vouchers to assist low income clients in paying their electric bills. He noted that LAP receives referrals from LES as well as local human service agencies and faith-based organizations. Hall also noted that customers who are struggling to pay their electric bills should contact LES.

Councilman Marvin asked LES to provide him information on: 1) LES' debt service target for 2008; 2) What LES' debt service coverage in 2008 would be if a rate increase is not approved; 3) The long term debt service coverage targets that have been discussed with the rating agencies; and, 4) The residential rates for a number of towns within 50 miles of Lincoln, excluding OPPD. He also asked if mild weather has affected LES' financial position. Bundy responded that LES is below budget on energy sales, largely due to lower sales earlier in the year. He noted that lower loads earlier in the year do not impact the bottom line as much as they do in the summer months. He noted that while retail sales are down, LES power costs are still substantially higher than budget.

Councilman Camp asked how much is in the budget for advertising. Bundy responded that it was a little more than $400,000, but he added that LES was canceling remaining advertising for 2008. He also asked if LES would continue to face these challenges in power costs in 2009. Bundy responded that the outlook for all energy sectors is one of increasing challenges and higher costs. He noted that we need to be looking at energy conservation and efficiency programs to help Lincoln residents deal with higher energy costs. He also noted that climate change legislation on the federal level would cause additional increases in LES costs.

Council Chair Eschliman asked if Perot Systems cited low electric rates as a driver for locating in Lincoln. Bundy responded that he was not aware if that was a factor for Perot Systems, but noted that the Lincoln Chamber of Commerce has indicated in the past that low electric rates have been an important factor for many businesses locating in Lincoln.

Terry Bundy thanked the Council members for their time to discuss the rate proposal. He noted that he understands that this will place additional cost pressures on Lincoln residents and businesses and that LES will continue to work with customers who are struggling. He indicated that even with a rate increase he expects LES rates to remain competitive. Chair Eschliman asked about identified reductions in economic development activities. Hall responded that LES will continue its work with the Chamber of Commerce on normal business expansion and retention activities. The reductions are related to more to some of the recruiting and prospecting activities that LES has supported through the Chamber.

Chair Eschliman excused LES from the meeting at approximately 11:00 a.m.

Respectfully Submitted,

BY: *S/Shelley R. Sahling-Zart*
Shelley R. Sahling-Zart
Assistant Secretary
LES Administrative Board

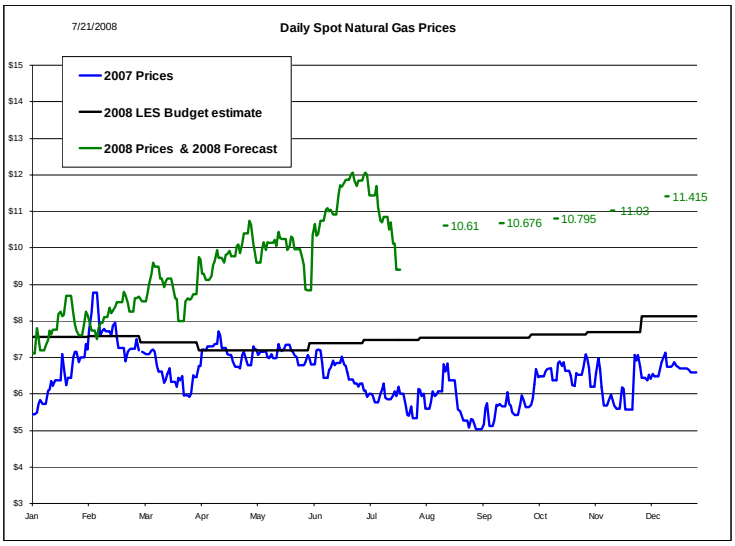
Exhibit I

2008 Rate Adjustment
September 2008

Background
and
LES Administrative Board
Proposal

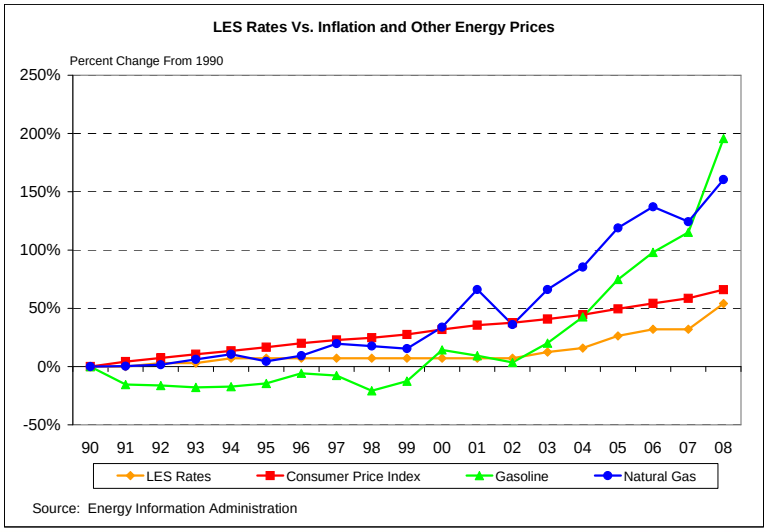
les.com

Natural Gas Volatility



les.com

CPI and Fuels

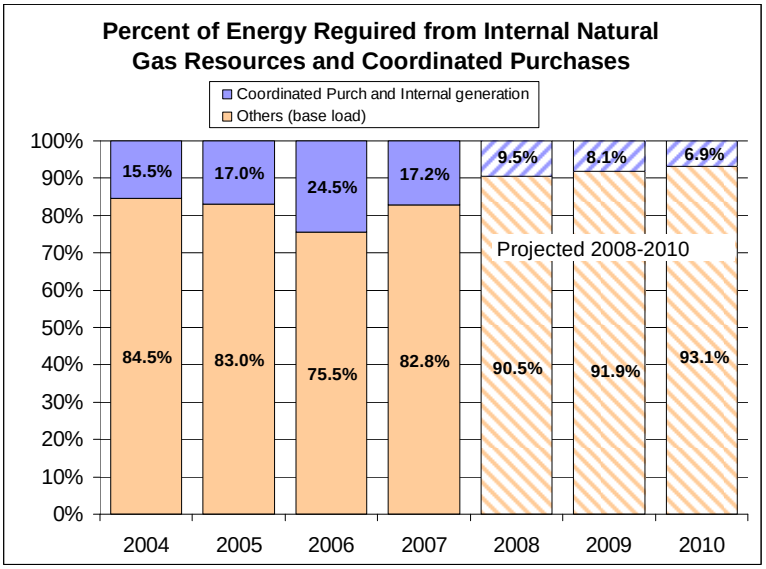


les.com

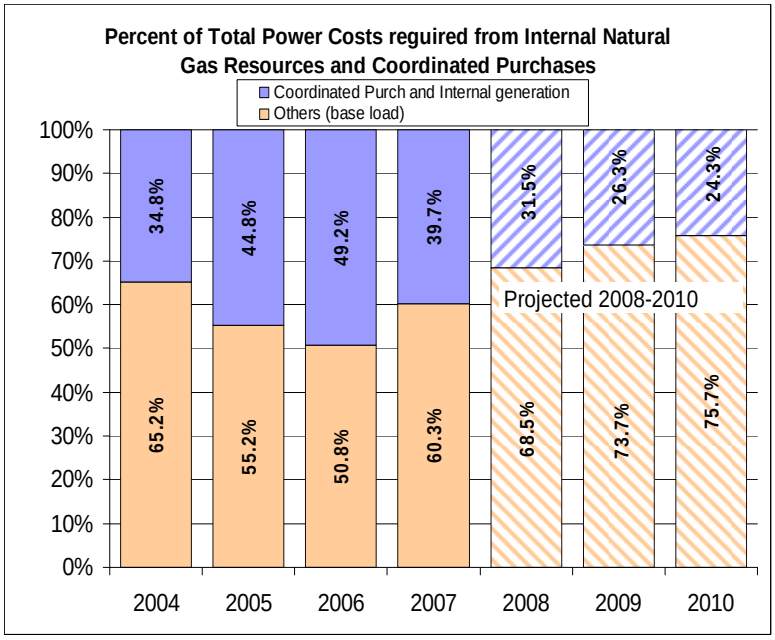
Volatility Around the Country

• OPPD	$90 million in 2009
• Denver	10% June, up 38% over '07
• Topeka	15% 2008
• Wichita	15% 2008
• St. Louis	12% + PCA
• Joplin, Mo	10% + PCA
• WAPA	14% 2009
• Tulsa	25% 2008
• Albuquerque	20%
• Austin	10%
• Reno	10%
• Portland	9%
• Atlanta	20%
• TVA	10%
• Charlotte	16%

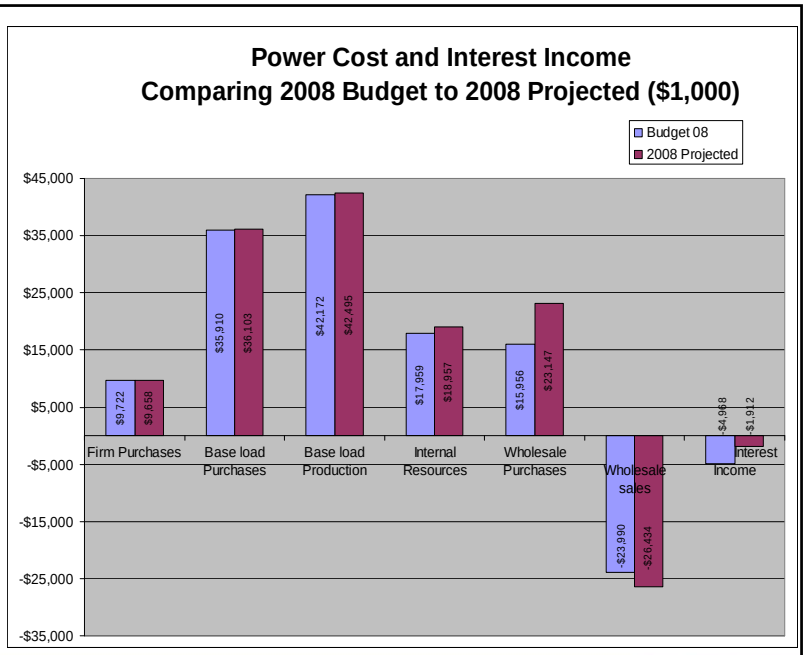
les.com



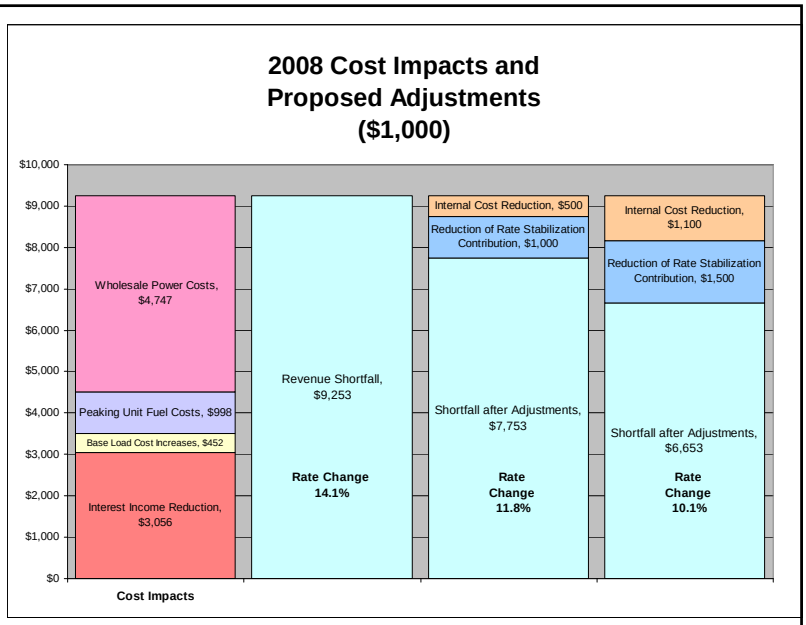
les.com



les.com



les.com



les.com

Rate Stabilization Use and Rates

Rate Stab.	Rate-Increase % 2008	Rate-Increase % 2009
• $1 Million	10.9%	0-3%
• $1.5 million	10.1%	1-4%
• $2 million	9.4%	2.5-5.5%
• $3 million	7.8%	4.5-7.5%
• $4 million	6.3%	7-10%

les.com

Timeline of Activity

August 5, 2008 - Public Meeting
- WAC Service Center 7:00 pm

August 8, 2008 - LES Administrative Board Meeting
- To consider Public Comments and Approve Final Rate Recommendation to forward to City Council

August 11, 2008 - First Reading LES Rate Resolution

August 18, 2008 - City Council Public Hearing and Consideration for Approval of Rate Adjustment

September 1, 2008 - New Rates are in effect

les.com

Exhibit II

2008 September Rate Adjustment
Internal Cost Reduction Summary

The LES Administrative Board, Budget and Rates Committee, has recommended the following reductions in planned expenditures for 2008. The reduction in expenditures identified reduces the current year rate increase percentage. The three major categories of expense reductions are listed below. Under each category there is a list of some larger items that can be cut or deferred to 2009. There are many more small items that make up the total. Beyond the items identified to date, LES managers will continue to look at all expenses as we go through 2008 with a goal of achieving a reduction of at least $1.1 million.

Labor Cost $130,000

Staff has identified positions which can be deferred to 2009. These hiring delays will not affect System safety (internal and public) nor will they affect System reliability. The representative list of positions included for deferral include IT Support ($23,000), Admin Support ($4,100), and Engineer ($41,000). Other positions include the deferred hiring of field forces until the 2009 budget year.

Travel and Training $250,000

Staff has identified training program previously scheduled or planned for the balance of 2008, and has canceled or deferred the staff participation. A summary listing of representative travel and training reductions for 2008 include IT technology support seminars and associated travel such as continued support of DB2, Itron, MS Tech Lotus Notes, ESRI, etc. ($42,500), a series of technical coursework and collaborative meetings on turbine management and generation efficiency ($21,650), Economic Development supporting activities ($6,500), commercial and industrial business seminars and advisory council ($6,500), continued training for the internal audit staff and associated travel ($18,000)

Purchases and Services $720,000

Staff has identified a number of deferral and/or reductions in software package purchases, consulting services, advertising and maintenance deferrals. These representative reductions include deferral of Carbon Footprint Calculator development with UNL Design Studio ($14,500), Advertising expenses for radio and print for conservation (35,000), market survey ($24,000) community education event ($24,000) digitalization of meter data files ($70,000), deferred equipment and property painting ($25,000), Alstom A inspections deferred to 2009 ($44,000), acquisition of E Billing services ($30,000), deferred facilities improvements (Asphalt repair, concrete repair, etc.) ($40,000).