

Color Coded Legend:

Policy and Procedure

Staffing

TRM

Storage of Documents

Additional Reporting

SCL Disagrees

Assessment and Recommendations

RISK MANAGEMENT CONTROLS DESIGN EFFECTIVENESS

The following section is a high-level overview assessment of the risk governance, transactional controls and credit risk components of SCL's risk infrastructure, based on our understanding of SCL's operations and prevalent energy industry practices. As indicated in this document, the assessment conducted is subjective and is based on potential gaps noted between current documented and described practices at SCL and our understanding of prevalent practices. Each of these categories has a formal structure that provides guidance to the SCL's functional operations. These protocols and guidelines are typically embodied in an organization's accepted Risk Management Policies and Procedures. Policies and procedures provide consistency and transparency in daily operational functions. Deloitte & Touche assessed the design element of SCL's risk policies and procedures to prevailing industry practice.

The risk infrastructure design components included in our analysis are shown in Table 1 below.

Table 1

A. Risk Governance	B. Transactional Controls	C. Credit Risk
▪ Risk Management Policy	▪ Risk Procedures	▪ Credit Risk Management

		Policy
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A. Risk Governance

This segment of our design assessment compared SCL's current risk management policies to our understanding of prevalent industry practices.

Prevalent Practice	SCL's Current Practice	Categorization	Recommendation	Management Response
A1- A RMP should establish guidelines for monitoring and controlling the financial risks related to the generation, supply, and marketing of electricity, and related hedging and trading activities and enforcing any deviations from policy.	SCL has a RMP for Wholesale Energy risk management activities. This policy defines the guidelines for monitoring and managing the risks of the organization associated with energy transacting and hedging activities.	✓	No recommendation at this time, as this appears to be generally in line with our understanding of Prevalent Practices.	
A2 - A RMP is designed to help ensure that the risks incurred are consistent with senior management's expectations.	SCL's RMP includes sections that describe the risk management and transacting philosophy of the company (primarily selling excess supply), the types of risk covered in the policy (including market price, credit / performance, volumetric, modeling, operations, and operational (commercial risk). Market and credit risk are described in additional detail and specifically mentioned as the two risk types where specific risk management approaches are developed. Additionally, the forward hedging strategies and controls are also detailed in the Policy.	✓	No recommendation at this time, as this appears to be generally in line with our understanding of Prevalent Practices.	
A3- A RMP includes a definition of the company's risk tolerance and transacting objectives.	The "Risk Management Philosophy" section of the RMP clearly defines the SCL's risk tolerance and transacting objectives, which are to manage the volatility in uncertainty of wholesale revenue and protect the interests of the ratepayers. The RMP also describes the 5% Tail Risk Metric which drives its forward hedging strategy and transacting objectives as well as the other various volumetric limits used to manage the risk of the organization.	✓	No recommendation at this time, as this appears to be generally in line with our understanding of Prevalent Practices.	
A4 - A RMP includes a definition of the major sources of risk.	SCL's RMP defines some of the various sources of risk such as market, credit/performance, volumetric, modeling, operations and operational risk. However, some risk types / risk sources	☞	SCL could consider revising its RMP with a broader and more complete set of risk definitions that encompass both current and potential future activities. Sample additional types of risk definitions to be included may consist	Agreed. SCL will address this by incorporating the recommendations into the next set of proposed changes to the RPM. Per the policy, any proposed changes to the Risk Management Policy put forth

Prevalent Practice	SCL's Current Practice	Categorization	Recommendation	Management Response
	<p>may be excluded or not explained at a level of detail desired. For example, market risk is mentioned but its components are not discussed (e.g., price, time spread, liquidity, basis and locational, option risk, and execution risk).</p> <p>This same observation was noted in the previous assessment and was agreed upon by SCL Management, but it does not appear that any changes were made to the Policy.</p>		<p>of: Administrative, Legal and Regulatory Risks.</p>	<p>by SCL are subject to approval by the Council.</p>
<p>A5 - A RMP includes a description of the roles and responsibilities and delegated authorities within the organization.</p>	<p>The RMP outlines the roles and responsibilities for several of the core functions in the risk governance structure, including the Superintendent, Chief Financial Officer ("CFO"), Risk Oversight Committee ("ROC"), PDM, and The Risk Oversight Director. The RMP does not define roles and responsibilities for the City Council (which can be considered the de facto Board of Directors). Additionally, the RMP does not define roles and responsibilities for the Accounting function.</p> <p>In addition, the Wholesale Energy Risk Management Procedures Manual ("Procedures Manual") includes descriptions of the roles and responsibilities for the Front, Middle, and Back Office functional groups but information does not match the Risk Management Policy and there is no organization chart for the Front Office (though there are organization charts for middle and back office).</p>		<p>SCL should consider documenting in the Risk Management Policy the roles and responsibilities of City Council related to Energy Risk Management.</p> <p>SCL should also consider having documented roles and responsibilities of the Accounting function in the Policy and make sure that information contained in the Policy (while less detailed) is the same as information contained in the procedures document.</p>	<p>Agreed.</p> <p>SCL will address this by incorporating the recommendations into the next set of proposed changes to the RPM. Per the policy, any proposed changes to the Risk Management Policy put forth by SCL are subject to approval by the Council.</p>
<p>A6 - A RMP includes the scope of authorized activities.</p>	<p>The RMP includes the scope of authorized activities. The Procedures Manual includes Authorized Products and Markets.</p> <p>The current scope of authorized activities included in the RMP does not include Renewable Energy Credits ("RECs"). This is a product type in which SCL has positions which should be measured and monitored under the scope of the RMP.</p> <p>While there is a REC Policy, the RMP does not make reference to this additional document and does not explicitly authorize trading in RECS and</p>		<p>SCL should consider including RECs within the scope of authorized activities and provide a link / mention of the established REC Policy that is currently in effect.</p> <p>SCL should also update the Policy to include the authorized market points of delivery to include the commonly used name of the trading location with linkage to sub-locations so that it is clear what is allowed or not allowed per Policy.</p>	<p>Agreed.</p> <p>SCL will address this by incorporating the recommendations into the next set of proposed changes to the RPM. Per the policy, any proposed changes to the Risk Management Policy put forth by SCL are subject to approval by the Council.</p>

Prevalent Practice	SCL's Current Practice	Categorization	Recommendation	Management Response
	<p>Greenhouse Gas / Carbon.</p> <p>Also, while the RMP does denote a list of authorized markets / trading locations, these do not currently match some of the detailed trading locations in the system of record (i.e. Northwest, Southwest, etc)</p> <p>Additionally, the list of authorized products contained in the RMP does not match the authorized products listed in the Procedures Manual.</p>		<p>SCL should also continue to evaluate current and planned transaction types for inclusion in the RMP.</p> <p>While the Procedures Manual should be more detailed, information contained in the Manual should be reflective of the information contained in the Policy and not have different authorized product types. In this way, SCL will have a common language across the documentation which should lead to a better understanding of the processes, procedures and authorized activities. SCL should reconcile these two documents to make sure there are no contradictions. SCL could also consider referencing information in one document in order to have consistency between the documents</p>	<p>Agreed.</p> <p>SCL will develop an internal work plan for incorporating the recommendations that relate to the Procedures Manual. This work plan will establish responsibility for completion, an expected timeline, and a mechanism for tracking progress towards that goal. Revisions to the Procedure Manual will be subject to final approval by the ROC to become effective.</p>
<p>A7- A RMP includes New Product Approval Process and Non-Standard Transaction Process.</p>	<p>While SCL's Procedures Manual includes a description of the type of information that the Power Management Executive should provide to start the New Product Approval process, the procedure does not document who is involved in the approval process, what specific personnel can approve new products, etc.</p>		<p>The Procedures document should be updated to provide a fuller description of not only the information that the Power Management Executive should provide, but should also document the process for review and approval of the new product.</p>	<p>Agreed.</p> <p>SCL will develop an internal work plan for incorporating the recommendations that relate to the Procedures Manual. This work plan will establish responsibility for completion, an expected timeline, and a mechanism for tracking progress towards that goal. Revisions to the Procedure Manual will be subject to final approval by the ROC to become effective.</p>
<p>A8- A RMP includes a summary of market and credit risk limits.</p>	<p>The RMP contains a summary of market risk limits related to volumes and the 5% Tail Risk metric. These market and volumetric risks include:</p> <p>A volumetric limit for not entering a month more than 50 a MW short.</p> <p>A volumetric limit for not selling more than 1,750,000 net forward contracts in any rolling 4 quarter period.</p> <p>A volumetric limit for not having a deficit in any forward quarter (rolling 4 quarter period) at the 50% confidence level.</p> <p>Credit risk limits are also described in the Procedures Manual.</p>		<p>SCL could consider developing additional risk limits for individual transactions (volumetric, notional value). This limit structure would serve as a delegation of authority for transacting personnel, setting specific limits for which a transaction would require approvals from the Manager, Power Management Executive, or ROC.</p>	<p>Disagree.</p> <p>SCL believes that the existing volumetric limits and clearly documented plans are transparent and provide sufficient oversight.</p>
<p>A9- A RMP includes Credit Risk Management and appropriate practices for managing counterparty credit risks.</p>	<p>The RMP includes a description of its Credit Risk Management practices with the specific details included in the</p>		<p>SCL could consider revising the Credit sections of the RMP and the Procedures Manual to reflect the</p>	<p>Agreed.</p> <p>SCL will address this by incorporating the recommendations into the next set</p>

Prevalent Practice	SCL's Current Practice	Categorization	Recommendation	Management Response
	<p>Procedures Manual.</p> <p>The Credit sections in the current versions of the RMP and the Procedures Manual do not accurately reflect the procedures performed as described by personnel performing the function.</p> <p>The Policy and Procedures do not define specifically how the credit analysis process can be used to move approved credit limits down from the Moody's KMV number and also do not reflect that the Senior Credit Analyst can lower credit limits for companies with no approval from the Risk Oversight Director or the CFO.</p>		<p>practices as currently performed.</p> <p>SCL should also consider modifying the process for credit limit assessments to where the Credit Analyst can lower credit limits based on a pre-determined percentage or dollar amount threshold with additional approvals beyond those limits provided by the Risk Oversight Director and CFO respectively.</p>	<p>of proposed changes to the RPM. Per the policy, any proposed changes to the Risk Management Policy put forth by SCL are subject to approval by the Council.</p> <p>SCL will develop an internal work plan for incorporating the recommendations that relate to the Procedures Manual. This work plan will establish responsibility for completion, an expected timeline, and a mechanism for tracking progress towards that goal. Revisions to the Procedure Manual will be subject to final approval by the ROC to become effective.</p>
<p>A10 - A RMP includes a description of the types, the frequency, and responsibilities for review and approval of internal and external reports generated and distributed.</p>	<p>The RMP includes a description of required risk reports that are submitted to the ROC, Superintendent, the Mayor and the City Council staff. The RMP lists the type, frequency, and distribution of these reports.</p> <p>The Procedures Manual contains a description of numerous additional reports and details the types, frequency, source, and distribution of reports to be developed by the Risk Oversight Director.</p>		<p>SCL should consider updating the Policy to include a fuller description of the various reports generated and distributed as well as examples of the format of the reports.</p> <p>SCL should also consider updating the documentation with the specific reports that will be generated and relied upon from the new Trading and Risk Management System.</p>	<p>Agreed.</p> <p>SCL will address this by incorporating the recommendations into the next set of proposed changes to the RPM. Per the policy, any proposed changes to the Risk Management Policy put forth by SCL are subject to approval by the Council.</p> <p>SCL will develop an internal work plan for incorporating the recommendations that relate to the Procedures Manual. This work plan will establish responsibility for completion, an expected timeline, and a mechanism for tracking progress towards that goal. Revisions to the Procedure Manual will be subject to final approval by the ROC to become effective.</p>
<p>A11 - A RMP includes a description of the Company's code of conduct and standards of compliance.</p>	<p>The RMP includes a compliance statement which employees must sign to acknowledge compliance with the RMP.</p> <p>The Procedures Manual describes the requirement of annual training for front, middle, and back offices to review the RMP and Procedures Manual in addition to SCL's Integrated Resource Plan ("IRP") and regulatory updates.</p>		<p>No recommendation at this time, as this appears to be generally in line with our understanding of Prevalent Practices.</p>	

B. Transactional Controls

This segment of our design assessment compared SCL’s documented transactional control procedure components to our understanding of prevalent industry practices.

Prevalent Practice	SCL’s Current Practice	Categorization	Recommendation	Management Response
B1 - Transaction Initiation procedures are described in detail within a formal procedural document	<p>Previously, prior to initiating deals, SCL Power Marketers created a deal approval sheet that described the intended transaction. The ROD met with the Power Marketers and approved the intended transaction after the deal was determined to meet the established frameworks of the WERM and the Procedures Manual.</p> <p>The SCL Power Marketers were responsible for entering wholesale energy transactions into the deal capture system of record, ACES.</p> <p>A set of procedures describing the pre-deal analysis methodology are provided in the Procedure Manual.</p> <p>This process is being changed by entering “dummy” deals into the Trading and Risk Management System which are then “stamped” by the Risk Oversight Division once the transaction is approved from a market and credit risk standpoint and compared against applicable hedging plans / strategies if applicable.</p>		No recommendation at this time for changes to the process) but process and procedures documentation should be updated to reflect the process as it is currently performed.	<p>Agreed.</p> <p>SCL will develop an internal work plan for incorporating the recommendations that relate to the Procedures Manual. This work plan will establish responsibility for completion, an expected timeline, and a mechanism for tracking progress towards that goal. Revisions to the Procedure Manual will be subject to final approval by the ROC to become effective.</p>
B2 – New Counterparty Approval procedures are described in detail within a formal procedural document	SCL has documented procedures describing its New Counterparty Approval process in the Procedure Manual.		No recommendation at this time, as this appears to be generally in line with our understanding of Prevalent Practices.	
B3 - Contract Administration procedures are described in detail within a formal procedural document	SCL does not have formal procedures that document the Contract Administration process		SCL should consider documenting the procedures that reflect valid enabling agreements and contracts are in place before SCL commits to a transaction or deal, and that reflect the terms of the contract are met throughout the life of the agreement.	<p>Agreed.</p> <p>SCL will develop an internal work plan for incorporating the recommendations that relate to the Procedures Manual. This work plan will establish responsibility for completion, an expected timeline, and a mechanism for tracking progress towards that goal. Revisions to the Procedure Manual will be subject to final approval by the ROC to become effective.</p>

Prevalent Practice	SCL's Current Practice	Categorization	Recommendation	Management Response
B4 - Credit Limit Extension procedures are described in detail within a formal procedural document	<p>The Procedure Manual references changes to counterparty's credit limit. The Credit sections in the current versions of the RMP and the Procedures Manual do not accurately reflect the procedures performed as described by personnel performing the function.</p> <p>The Policy and Procedures do not define specifically how the credit analysis process can be used to move approved credit limits down from the Moody's KMV number and also do not reflect that the Senior Credit Analyst can lower credit limits for companies with no approval from the Risk Oversight Director or the CFO. .</p>		<p>SCL could consider revising the Credit sections of the RMP and the Procedures Manual to reflect the practices as currently performed.</p> <p>SCL should also consider modifying the process for credit limit assessments to where the Credit Analyst can lower credit limits based on a pre-determined percentage or dollar amount threshold with additional approvals beyond those limits provided by the Risk Oversight Director and CFO respectively.</p>	<p>Agreed.</p> <p>SCL will develop an internal work plan for incorporating the recommendations that relate to the Procedures Manual. This work plan will establish responsibility for completion, an expected timeline, and a mechanism for tracking progress towards that goal. Revisions to the Procedure Manual will be subject to final approval by the ROC to become effective.</p>
B5 - New Product Approval procedures are described in detail within a formal procedural document	<p>While SCL's Procedures Manual includes a description of the type of information that the Power Management Executive should provide to start the New Product Approval process and the procedures, the procedure does not document who is involved in the approval process, what specific personnel can approve new products, etc.</p>		<p>The Procedures document should be updated to provide a fuller description of not only the information that the Power Management Executive should provide, but should also document the process for review and approval of the new product.</p>	<p>Agreed.</p> <p>SCL will develop an internal work plan for incorporating the recommendations that relate to the Procedures Manual. This work plan will establish responsibility for completion, an expected timeline, and a mechanism for tracking progress towards that goal. Revisions to the Procedure Manual will be subject to final approval by the ROC to become effective.</p>
B6 - Transaction Execution procedures are described in detail within a formal procedural document	<p>SCL has documented procedures that describe the Term, Day Ahead, Balance of the Month, Prompt Month, and Real Time transaction execution process at a relatively high level.</p> <p>These procedures, particularly for real time transacting do not adequately describe the specific process and the control points and are not to the level of detail of other processes described in the procedures document.</p>		<p>SCL should consider more fully documenting the procedures around the transaction execution process to reflect how the process is currently performed. The documented practices should include at least the following:</p> <ul style="list-style-type: none"> - a list of approved products and market delivery points - description of trade entry into the system - counterparty validation process - deal validation - deal amendment processes 	<p>Agreed.</p> <p>SCL will develop an internal work plan for incorporating the recommendations that relate to the Procedures Manual. This work plan will establish responsibility for completion, an expected timeline, and a mechanism for tracking progress towards that goal. Revisions to the Procedure Manual will be subject to final approval by the ROC to become effective.</p>
B7 - Tape Recording and Monitoring procedures are described in detail within a formal procedural document	<p>SCL currently records all transactions executed over taped phone lines at their Seattle, Washington office. SCL has procedures describing the taped recording, monitoring and archiving processes.</p>		<p>No recommendation at this time, as this appears to be generally in line with our understanding of Prevalent Practices.</p>	

Prevalent Practice	SCL's Current Practice	Categorization	Recommendation	Management Response
<p>B8 - Market Data Collection and Integrity procedures are described in detail within a formal procedural document</p>	<p>Based upon interviews with SCL staff, it appears that IT staff currently downloads prices automatically into both the Power Ops and the ETRM systems from PM Portal on a weekly basis. There are no "sanity checks" (aka independent price validations to make sure that prices are within an expected range) currently being applied to the data being downloaded (abnormally large % deviations, unusually high week-over-week price changes, missing prices, etc.).</p> <p>Additionally, the price reporting procedure for reporting to index developers is not adequately documented in the Procedures Manual.</p>		<p>SCL should consider developing a more formal price curve download methodology including detective price curve validation.</p> <p>SCL could also adopt a methodology for the submission of data curves constructed by the ROD. To determine accuracy of data submitted to market price indicia publishers, the methodology could include:</p> <ul style="list-style-type: none"> - processes on the appropriate data to provide - process on the verification that data is timely, correct, and auditable - process to determine the data will remain confidential, independent and objective - process to determine the data is consistent, timely and regular <p>SCL should make efforts to document the aforementioned processes and procedures in the Procedures Manual and staff this function accordingly.</p>	<p>Agreed.</p> <p>SCL will develop an internal work plan for incorporating the recommendations that relate to the Procedures Manual. This work plan will establish responsibility for completion, an expected timeline, and a mechanism for tracking progress towards that goal. Revisions to the Procedure Manual will be subject to final approval by the ROC to become effective.</p> <p>The process is currently underway to fill two vacant positions within the Risk Oversight Division. The skills being sought will greatly strengthen the ROD in this area.</p>
<p>B9 - Confirmations (Written and Oral) procedures are described in detail within a formal procedural document</p>	<p>SCL's Power Marketers are responsible for generating confirmations from the system.</p> <p>SCL has documented the process for confirmations of all sales transactions in the WERM Procedure Manual.</p> <p>This finding was noted in the previous assessment report and SCL Management made a conscious decision to not change the process as there is the desire to have accountability for transactions residing in the front-office.</p>		<p>The ROD should consider taking ownership of the confirmation process from confirmation generation to record keeping and retention.</p> <p>SCL should consider utilizing one central and common database of record to assist in generating and receiving counterparty confirmations. A centralized database would improve data measurement and management throughout the transaction lifecycle, minimize errors and reduced lost data, as well as streamline data requests for both internal and external reporting and assessments.</p>	<p>Agreed.</p> <p>SCL will develop an internal work plan for incorporating the recommendations that relate to the Procedures Manual. This work plan will establish responsibility for completion, an expected timeline, and a mechanism for tracking progress towards that goal. Revisions to the Procedure Manual will be subject to final approval by the ROC to become effective.</p>
<p>B10 - Invoicing and Settlement procedures are described in detail within a formal procedural document</p>	<p>The ROD - Settlement group is responsible for transaction settlement activities. The WERM Procedure Manual in Exhibit "G" describes the expectations of the Settlement group and each of the wholesale counterparties. The procedures also describe the expectations when disagreements take place between SCL and counterparties over quantity or transaction price.</p>		<p>No recommendation at this time, as this appears to be generally in line with our understanding of Prevalent Practices.</p>	<p>Agreed.</p> <p>SCL will develop an internal work plan for incorporating the recommendations that relate to the Procedures Manual.</p>

Prevalent Practice	SCL's Current Practice	Categorization	Recommendation	Management Response
	In addition, the ROD - Settlement group has a set of procedures in a document titled Monthly Checkout & Settlement Policy. As the process is currently in transition based on the new system, processes and procedures are in flux.		Once the system is fully in place and functioning as expected, processes and procedures should be updated to reflect the new process.	This work plan will establish responsibility for completion, an expected timeline, and a mechanism for tracking progress towards that goal. Revisions to the Procedure Manual will be subject to final approval by the ROC to become effective.
B11- Management Reporting procedures are described in detail within a formal procedural document	SCL has documented procedures describing its Management Reporting process in the WERM and in the Procedure Manual.		No recommendation at this time, as this appears to be generally in line with our understanding of Prevalent Practices.	

C. Credit Risk Management

This segment of our design assessment compared SCL's current credit risk management policies to our understanding of industry prevalent practices.

Prevalent Practice	SCL's Current Practice	Categorization	Recommendation	Management Response
C1 - Organizations' risk management infrastructure will always include a Credit policy, which memorializes the organization's Credit controls to mitigating the inherent risks associated with commodity transacting activities.	The Credit Policy is included as a section of the RMP. The Procedures Manual describes the organization's credit controls and processes but the current documentation does not match with the processes and procedures currently being performed by the Credit Analyst		SCL should consider modifying the documentation for the credit assessment processes and controls to reflect the way in which the process is being performed.	Agreed. SCL will develop an internal work plan for incorporating the recommendations that relate to the Procedures Manual. This work plan will establish responsibility for completion, an expected timeline, and a mechanism for tracking progress towards that goal. Revisions to the Procedure Manual will be subject to final approval by the ROC to become effective.
C2 - At a minimum, risk policies document the structure, processes, controls, and systems to manage market and credit risk.	SCL's Credit Policy and Procedures describe the credit risk control structure, credit management processes and controls, but the current documentation does not match with the processes and procedures currently being performed by the Credit Analyst		See recommendation above.	Agreed. SCL will develop an internal work plan for incorporating the recommendations that relate to the Procedures Manual. This work plan will establish responsibility for completion, an expected timeline, and a mechanism for tracking progress towards that goal. Revisions to the Procedure Manual will be subject to final approval by the ROC to become effective.

Prevalent Practice	SCL's Current Practice	Categorization	Recommendation	Management Response
C3 - Organizations design one comprehensive credit policy to make the maintenance and administration responsibilities more manageable.	SCL's credit policy describes its credit controls and processes related to the transacting activities of the Power Marketing function, (i.e., energy transactions with a term of less than 24 months), however there is no policy or procedure documentation describing credit evaluation for longer term contracts. The credit evaluation of long term contracts was described to us as being a requirement; however there does not appear to be any documentation of this credit evaluation.		SCL could consider revising its Credit Policy to include its credit risk tolerance, credit monitoring and mitigation controls, limit structure, and reporting requirements related to long term contracts. The Procedures Manual could also include documentation which formalizes the credit approval process for long term contracts.	Agreed. SCL will develop an internal work plan for incorporating the recommendations that relate to the Procedures Manual. This work plan will establish responsibility for completion, an expected timeline, and a mechanism for tracking progress towards that goal. Revisions to the Procedure Manual will be subject to final approval by the ROC to become effective.
C4 - Once a credit policy is approved, all relevant transacting personnel are required to acknowledge in writing that they have been informed of and understand the policies. The policies and amendments should be announced in a timely manner and be readily accessible to each employee by hard or electronic copy. All relevant trading personnel should be required to reaffirm the policies annually.	The Credit Policy is included in the RMP which requires all transacting and control personnel to sign a Statement of Compliance indicating that they have read, understood and agree to comply with the RMP and the Procedures Manual.		No recommendation at this time, as this appears to be generally in line with our understanding of Prevalent Practices.	
C5 - A comprehensive credit policy should include, at a minimum: A credit risk tolerance statement and policy objectives; Identification of credit risk exposures (e.g., pre-settlement, settlement, current exposure, potential exposure), sources and mitigation techniques; Delegated credit authorities and approvals, including clearly defined credit personnel roles and responsibilities, reporting lines and an illustration of the credit organization structure	SCL's Credit Policy includes a credit risk management philosophy statement. SCL's Credit Policy includes descriptions of credit risk exposures or sources. It also describes credit risk mitigation techniques such as authorized credit enhancements and various credit management processes The Procedures Manual describes the approval process for setting credit limits as well as a description of credit personnel roles and responsibilities.		No recommendation at this time, as this appears to be generally in line with our understanding of Prevalent Practices.	
The credit risk assessment methodology including scoring models, qualitative and quantitative analysis, and internal credit ratings;	The Procedures Manual version 06182010 includes a description of a credit scoring model, however the description does not go into an appropriate level of detail as to how the credit scoring methodology is performed. It is our understanding that the scoring methodology starts with the		SCL should update the Procedures Manual to include a more complete and accurate description of the current credit scoring methodology. SCL should also consider monitoring the performance of their counterparties against the assigned credit rating.	Agreed. SCL will develop an internal work plan for incorporating the recommendations that relate to the Procedures Manual. This work plan will establish responsibility for completion, an expected timeline, and a mechanism for tracking progress towards that goal.

Prevalent Practice	SCL's Current Practice	Categorization	Recommendation	Management Response
Acceptable forms of credit support (credit enhancement);	credit ratings assigned by Moody's KMV and then modifies this score based on quantitative and qualitative reviews performed by the Credit Analyst. SCL's Credit Policy includes a description of acceptable forms of credit enhancement.	✓	No recommendation at this time, as this appears to be generally in line with our understanding of Prevalent Practices.	Revisions to the Procedure Manual will be subject to final approval by the ROC to become effective.
Document retention and file standards;	The Procedures Manual includes a description of the Credit File Maintenance process, which describes the required contents for each credit file and describes document retention standards. However, the credit files and enhancements (i.e. Letters of Credit, etc) are not maintained in a centralized, fire-proof, storage location.	👉	SCL should take efforts to have credit enhancement documentation is maintained in a secure and fire-proof storage environment.	Agreed. Implementation underway.
Credit risk reporting standards including report owner, frequency, and distribution; and	The Procedures Manual states that the Credit Risk Analyst will prepare a weekly credit exposure report for the ROC.	✓	No recommendation at this time, as this appears to be generally in line with our understanding of Prevalent Practices.	
Policy maintenance and administration requirements.	The Credit Policy is included in the RMP which requires an annual review by the ROC. Potential changes are recommended for approval to the Superintendent.	✓	No recommendation at this time, as this appears to be generally in line with our understanding of Prevalent Practices.	

RISK MANAGEMENT CONTROLS OPERATING EFFECTIVENESS

In an effort to facilitate effective risk management controls, certain risk management infrastructure categories should not only be designed and in place, but also operationally consistent. This evaluation focused on three primary risk categories: Risk Governance, Transactional Control and Credit Risk Management. These categories are generally considered a first tier of the risk framework hierarchy and are typically part of a well designed risk infrastructure. Each category is typically comprised of risk control activities that, when grouped together, form a discrete group of what can be referred to as "risk control components." Components typically form the second tier of a risk framework hierarchy and are generally considered fundamental business practices that help establish a sound risk management foundation and assess operating effectiveness. Deloitte & Touche utilized a broad set of risk control components that we believe apply to the current nature, size and complexity of SCL's energy transacting function and related transaction activity support areas for purposes of this evaluation. The below list includes typical risk control components within an organization.

The risk control components aligned by each high-level category are shown in Table 2 below.

Table 2

Risk Governance	Transactional Controls	Credit Risk
<ul style="list-style-type: none"> ▪ Risk Management Committee ▪ Roles & Responsibilities ▪ Book Structure ▪ Qualitative Limits ▪ Quantitative Limits ▪ Exposure Monitoring ▪ Reporting ▪ Code of Conduct 	<ul style="list-style-type: none"> ▪ Pre-Deal Processes and Authorization ▪ Deal Execution ▪ Deal Capture ▪ Deal Entry Validation ▪ Contract Administration ▪ Confirmation ▪ Settlements 	<ul style="list-style-type: none"> ▪ Credit Oversight ▪ Credit Policy ▪ Credit Documentation ▪ Counterparty Assessment ▪ Limit Setting ▪ Credit Risk Measurement ▪ Credit Enhancements ▪ Exposure Monitoring ▪ Collections

A. Risk Governance

Prevalent Practice	SCL's Current Practice	Categorization	Recommendation	Management Response
1.				
<p>1.1 – The RMC is composed of members from Management that are familiar with and have a detailed understanding of energy activities and their associated risks. RMC members may include:</p> <ul style="list-style-type: none"> – CRO – Chief (Executive) Administrative Officer – Chief Financial Officer – Head of Transacting – Middle and Back Office Functions. – Legal and/or Regulatory 	<p>SCL's ROC is comprised of the following SCL employees:</p> <ul style="list-style-type: none"> • CFO (Chair) • Power Supply and Environmental Affairs Officer • Risk Oversight Director • Director of Power Operations & Marketing (non-voting) • Director of Power Contracts & Resource Acquisition (non-voting) 		<p>SCL should consider expanding the ROC to add voting representation from the Back Office (for instance the Controller) and personnel from Legal / Regulatory. Many potential risk aspects such as increased regulatory oversight and new accounting rules can extend into these areas and having additional perspective could lead to decisions with greater insight into the various risk aspects of a transaction or new product.</p>	<p>Disagree. SCL feels that the current makeup of the ROC provides sufficient business perspective to identify risks. The ROC can, and does, bring in other disciplines as needed on a guest basis to consult on specific issues. The administrative difficulties of coordinating the schedules of a larger pool of senior staff would likely lead to members not consistently being available and a loss of continuity of action and decision making within the ROC from meeting to meeting that currently exists.</p>
<p>1.2 - The RMC is responsible for understanding of risk management concepts.</p>	<p>The ROC reviews risk reports on a weekly basis which describe SCL's compliance with risk limits, risk metrics, hedging plans, credit exposures, and market information.</p>		<p>No recommendation at this time, as this appears to be generally in line with our understanding of Prevalent Practices.</p>	

Prevalent Practice	SCL's Current Practice	Categorization	Recommendation	Management Response
	<p>In addition, the ROC meets on a bi-weekly basis at a minimum, and more often if circumstances or events warrant additional meetings, to discuss SCL's transacting activities and risk exposures. Members of the ROC actively discuss risk management concepts during these meetings.</p>			
<p>1.3 - The RMC should be responsible for setting corporate policies and guidelines for risk management and measurement.</p>	<p>The ROC is responsible for reviewing the RMP annually and providing recommendations for the Superintendent's, City Council's and the Mayor's approval annually.</p> <p>The ROC is also responsible for reviewing and approving the Procedures Manual, as well as risk management strategies and hedging plans to be executed by the front office.</p>		<p>No recommendation at this time, as this appears to be generally in line with our understanding of Prevalent Practices.</p>	
<p>1.4 - The RMC is responsible for overseeing and reviewing the risk management process and infrastructure.</p>	<p>The ROC is responsible for reviewing and approving the Procedures Manual which describes the risk management control processes and infrastructure.</p> <p>While the ROC has responsibility for review and approval of the Procedures Manual, the Manual does not appear to be consistent in the level of detail, level of completeness and accuracy in describing how the various front, middle and back office processes, procedures and controls are currently performed.</p> <p>Particular areas noted where enhanced documentation would be helpful are Transaction Execution, Credit Approval, and Settlements.</p>		<p>SCL should consider performing a detailed assessment of the Procedures Manual in light of the updating of numerous processes based on personnel changes, implementation of the new Trading and Risk Management System and resulting modifications to processes, procedures and controls.</p> <p>SCL should establish an agreed upon level of detail for describing these processes, procedures and controls and provide a template for documentation in order to have consistency across the various functional areas regarding the documentation of the various work activities.</p>	<p>Agreed.</p> <p>SCL will develop an internal work plan for incorporating the recommendations that relate to the Procedures Manual. This work plan will establish responsibility for completion, an expected timeline, and a mechanism for tracking progress towards that goal. Revisions to the Procedure Manual will be subject to final approval by the ROC to become effective.</p>
<p>1.5 - The RMC is responsible for reviewing and approving risk limits.</p>	<p>The ROC must submit a request to the Superintendent for approval for all risk limit changes. These requested changes, upon approval by the Superintendent, are also submitted to the City Council's Energy, Technology, & Civil Rights Committee (ETCRC) for review and approval at the time the request is made.</p> <p>Any risk limit modifications made throughout the year are reviewed and reaffirmed by the ETCRC on an annual basis.</p>		<p>No recommendation at this time, as this appears to be generally in line with our understanding of Prevalent Practices.</p>	

Prevalent Practice	SCL's Current Practice	Categorization	Recommendation	Management Response
1.6 - The RMC is responsible for ensuring that proper controls are in place.	The ROC is responsible for approving and implementing the procedures contained in the Procedures Manual which establishes the general control process with regards to risk management.		See comment In Section 1.4 above.	Agreed. SCL will develop an internal work plan for incorporating the recommendations that relate to the Procedures Manual. This work plan will establish responsibility for completion, an expected timeline, and a mechanism for tracking progress towards that goal. Revisions to the Procedure Manual will be subject to final approval by the ROC to become effective.
1.7 - The RMC is responsible for understanding and approving methodologies used to measure and control risk taking.	The ROC regularly discusses SCL's risk metrics at its bi-weekly meetings The Finance Group previously committed to address several recommendations for improvements to the risk model as a result of an assessment performed in 2008. Several items have been completed, with progress made on other items. However, these improvements have not been completed as planned as a result of availability of quantitative resources due to conflicting priorities.		SCL may consider investing in additional quantitative resources in order to support the risk modeling activities. There appears to be misalignment of responsibility and authority related to developing and monitoring the risk metrics. SCL should revisit the findings of the previous report and make a final determination on how to address the recommendations. Currently, the Risk Oversight Director holds the responsibility to produce the risk reports including compliance with the risk metric; however he does not have authority to direct and assign quantitative staff to focus on the model. SCL could consider developing a more quantitative skill set within the ROD in order to support the risk metric calculation as well as other model validation and reporting requirements.	Agreed. The process is currently underway to fill two vacant positions within the Risk Oversight Division. The skills being sought will strengthen the ROD in this area. However, quantitative skills are available in the utility's Financial Planning area. The manager of that unit is the leader of the Risk Working Group, and has responsibilities for work of this nature.
1.8 - The RMC is responsible for reviewing and approving exceptions and amendments to policies.	The ROC is responsible for reviewing the RMP on an annual basis and recommending changes to the Superintendent for approval. The official version of RMP is not currently secured in a folder or area that is only accessible to authorized personnel. This leads to the possibility that unauthorized changes could be made to the Policy that are not "caught" during the annual review process.	 	No recommendation at this time, as this appears to be generally in line with our understanding of Prevalent Practices SCL should consider securing the official version of the RMP in an area that is accessible to only pre-determined, authorized personnel. All versions of the RMP that are distributed to personnel should be read only or PDF versions.	Agreed. Implementation of this recommendation is currently underway.
1.9 - The RMC is responsible for evaluating portfolio risk.	The ROC receives weekly risk reports and meets on a bi-weekly basis to monitor and evaluate portfolio risk.		No recommendation at this time, as this appears to be generally in line with our understanding of Prevalent Practices.	
1.10 - The RMC is responsible for meeting as least monthly or more frequently as necessary to discuss risk management related items.	The ROC meets at least twice per calendar month. In addition, any member of the ROC has the ability to call an emergency meeting.		No recommendation at this time, as this appears to be generally in line with our understanding of Prevalent Practices.	

Prevalent Practice	SCL's Current Practice	Categorization	Recommendation	Management Response
2.				
<p>2.1 - Organizations should have clearly delineated roles and responsibilities by functional area.</p>	<p>The Procedures Manual describes the high level roles and responsibilities of the Front, Middle, and Back Offices.</p> <p>There do appear to be instances where the current roles and responsibilities preclude the development of independent reporting.</p>		<p>SCL could consider re-evaluating the alignment of certain roles and responsibilities to establish a more controlled environment. SCL should clearly document and communicate these roles and responsibilities across the organization.</p> <p>Specific areas which SCL should consider include:</p> <ul style="list-style-type: none"> - Confirmations - Risk Metric calculations - MTM valuation - Independent validation of generation forecasts 	<p>Agreed.</p> <p>Staffing limitations and existing vacancies have led to less than optimal segregation of duties. Efforts are underway to fill vacancies within the Risk Oversight Division and once complete, SCL will re-evaluate the distribution of workload to address any shortcomings identified.</p>
<p>2.2 - Organizations should have clearly delineated authorities and approvals by functional area.</p>	<p>The Procedures Manual describes the delegation of authority consistent with Seattle Municipal Code 21.49.130.B.2 which authorizes SCL to enter into energy transactions with a term of not more than 24 months. The procedures manual segments this delegation of authority by Front Office desk, defining the specific tenors authorized for transactors on the Forward, Daily, and Real-Time desks.</p>		<p>SCL could consider further refining its delegation of authority to include varying degrees of authorized volumetric or notional amounts by level. This limit structure would serve to trigger communication from the trader to the desk manager, Power Management Executive, or ROC dependent on the size of the potential transaction.</p>	<p>Disagree.</p> <p>SCL believes that the existing volumetric limits and clearly documented plans are transparent and provide sufficient oversight.</p>
3.				
<p>3.1 - Organizations with varying transacting activities should have a Book Structure that segments the corporate transacting portfolio into sub-portfolios, according to the role of the transactions in the business strategy, and the risks inherent in that transacting strategy.</p>	<p>SCL does not currently have a book structure in place but is working on implementing a book structure once the new Trading and Risk Management system is fully functional. SCL's transacting activities include both hedging activities and "re-balancing" activities to manage differences in surplus forecasts throughout the year.</p> <p>Over the past two years (during the time of our assessment) transactions were captured in the ACES scheduling system without designation of a book or transacting strategy.</p> <p>Once the TRM system is fully operational, it is expected that the transactions will be entered into one of the three delineated books:</p> <p style="text-align: center;">Resource book - Long-term</p>		<p>SCL should continue moving forward in the designing and implementing of the book structure to segment its transacting activities into sub-portfolios in order to measure and monitor performance and risk exposures associated with each transacting strategy.</p> <p>This would enable additional reporting, such as performance reporting by transacting strategy or business line.</p> <p>SCL should also consider whether they would provide value to have sub-books within the book structure to monitor positions by trading location / hub.</p> <p>Additionally, SCL should formally document the book structure in the Policy and Procedures documentation.</p>	<p>Agreed.</p> <p>The TRM system currently being implemented provided book structure.</p> <p>Agreed.</p> <p>SCL will evaluate the potential benefit of sub-book structure in monitoring the operations of our business.</p> <p>Agreed.</p> <p>SCL will develop an internal work plan for incorporating the recommendations that</p>

Prevalent Practice	SCL's Current Practice	Categorization	Recommendation	Management Response
	<p>transactions such as wind generation, hydro forecast, etc</p> <p>Marketing book – balancing between resource book and load. This includes hedging and re-balancing transactions.</p> <p>Operations book – Includes prompt month transactions and closer, including day-ahead and real-time transactions.</p>			<p>relate to the Procedures Manual. This work plan will establish responsibility for completion, an expected timeline, and a mechanism for tracking progress towards that goal. Revisions to the Procedure Manual will be subject to final approval by the ROC to become effective.</p>
<p>3.2 - The Risk Policy contains a description of transactions to be included in each book, practices for transferring transactions from one book to another, and approval required to create a new book.</p>	<p>SCL does not currently have a book structure in place. The RMP does include a description of the products authorized for transacting, but does not distinguish between different transacting strategies, nor does it describe the practices for transferring transactions between books or the process and approval required to create new books within the book structure.</p>		<p>SCL should consider updating its RMP to include a description of transactions included in each book as well as a risk limit structure which is consistent with its risk tolerance for each type of transacting activity.</p>	<p>Agreed.</p> <p>SCL will address this by incorporating the recommendations into the next set of proposed changes to the RPM. Per the policy, any proposed changes to the Risk Management Policy put forth by SCL are subject to approval by the Council.</p>
<p>3.3 - Those responsible for executing transactions appropriately designate the correct book when the transaction is entered into.</p>	<p>See description in Section 3.1 above.</p>		<p>SCL should consider assigning responsibility to transacting personnel to tag each transaction with the appropriate book in the system of record and formally document this process in the RMP and/or Procedures documentation.</p>	<p>Agreed.</p> <p>SCL will develop an internal work plan for incorporating the recommendations that relate to the Procedures Manual. This work plan will establish responsibility for completion, an expected timeline, and a mechanism for tracking progress towards that goal. Revisions to the Procedure Manual will be subject to final approval by the ROC to become effective.</p>
<p>4.</p>				
<p>4.1 - Qualitative limits define the commodities, geographic locations, instrument types and tenors that are approved for trading.</p>	<p>Seattle Municipal Code 21.49.130.B.2 authorizes SCL to transact in energy for a tenor of not more than 24 months.</p> <p>The RMP includes authorized delivery points and authorized transaction types with approved tenors.</p> <p>The RMP and Procedures documents are not completely consistent and accurate in their documentation of authorized "delivery locations" (as defined in the RMP), "markets" (as defined in the Procedures document), and the trading hubs set up in the system of record. Certain hubs (such as NW / SW) are listed in the trading system but are not defined in either the Policy (as "Delivery Points") or</p>		<p>SCL should consider revising its Policy and Procedures documentation to be consistent in the terminology and vernacular used in describing the limitations placed on the business.</p> <p>SCL should focus on the particular items noted in the current practice description, but also assess the documentation for completeness, consistency and accuracy as the processes, controls and procedures change in conjunction with implementation of the new system.</p>	<p>Agreed.</p> <p>SCL will develop an internal work plan for incorporating the recommendations that relate to the Procedures Manual. This work plan will establish responsibility for completion, an expected timeline, and a mechanism for tracking progress towards that goal. Revisions to the Procedure Manual will be subject to final approval by the ROC to become effective.</p>

Prevalent Practice	SCL's Current Practice	Categorization	Recommendation	Management Response
	Procedures (as "Markets), though they are well understood transacting points within the industry and by SCL personnel.			
4.2 - The limits are approved by the RMC, and typically are contained in the Risk Management Policy.	<p>The tenor, geographic location and transaction type limits are included in the RMP and approved by the Superintendent and the City Council of the City of Seattle on the recommendation of the ROC.</p> <p>The Delegation of Authority is recommended by the Power Management Executive and approved by the Superintendent.</p>	✓	No recommendation at this time, as this appears to be generally in line with our understanding of Prevalent Practices.	
5.				
5.1 - Quantitative limits exist such that exposures are monitored and reported against the limits, so that senior management can assess compliance with the stated risk tolerance.	SCL has three volumetric limits (prompt month, forward month's resource requirement, and forward sales limit) as well as risk metric tolerance limits which are monitored and reported on a weekly basis to the ROC and senior management to assess compliance.	✓	No recommendation at this time, as this appears to be generally in line with our understanding of Prevalent Practices.	
5.2 - The RMC should expect the transacting function to manage exposures so that they stay within limits at all times, or else explain why it is not possible to remain within the limits. These limits would have application for all aspects of an organization's transacting risk.	<p>The PMD is expected to manage SCL's exposures within the approved risk limits. When these limits are violated (which recently has been more related to changes in forecasts or other variables, rather than transacting activity) the reason for the violation is noted in the ROC Meeting Minutes and corrective action is agree on.</p> <p>The Power Management Executive submits a written hedging strategy each year and several hedging plans throughout the year. These strategies/plans describe the transacting intentions of the PMD relative to the risk limits. However, there are numerous modifications made to this plan throughout the year which do not appear to have as rigorous documentation and approval. Many of these approvals were email exchanges which often showed transactions that were executed, but not necessarily explicit approval.</p>	<p>✓</p> <p>👉</p>	<p>No recommendation at this time, as this appears to be generally in line with our understanding of Prevalent Practices.</p> <p>SCL should consider taking action to more formally document all changes, modifications and approval to hedge plans and keep these changes with the original hedging strategy and plans.</p>	<p>Agreed.</p> <p>SCL will develop an internal work plan for incorporating the recommendations that relate to the Procedures Manual. This work plan will establish responsibility for completion, an expected timeline, and a mechanism for tracking progress towards that goal. Revisions to the Procedure Manual will be subject to final approval by the ROC to become effective.</p>

Prevalent Practice	SCL's Current Practice	Categorization	Recommendation	Management Response
<p>5.3 - Quantitative limit structures specify the risk limits that are applied to each sub-portfolio. Limits can be structured in a number of ways including:</p> <ul style="list-style-type: none"> - Limits on Nominal Open Positions (e.g., MW); - Tenor/Duration Limits on transactions; - Limits associated with stress testing & Scenario analysis; and - "At Risk" Measures (Cash flow at-Risk, Earnings-at-Risk). 	<p>SCL's RMP includes risk limits on nominal open positions for various time periods, duration limits on transactions, and the 5% Tail Risk metric.</p> <p>These market and volumetric risks include:</p> <p>A volumetric limit for not entering a month more than 50 a MW short.</p> <p>A volumetric limit for not selling more than 1,750,000 net forward contracts in any rolling 4 quarter period.</p> <p>A volumetric limit for not having a deficit in any forward quarter (rolling 4 quarter period) at the 50% confidence level.</p> <p>SCL currently does not have in place any volumetric or notional limits on individual transactions.</p>		<p>SCL could consider developing additional risk limits for individual transactions (volumetric, notional value). This limit structure would serve as a delegation of authority for transacting personnel, setting specific limits for which a transaction would require approvals from the Manager, Power Management Executive, or ROC.</p>	<p>Disagree.</p> <p>SCL believes that the existing volumetric limits and clearly documented plans are transparent and provide sufficient oversight.</p>
6.				
<p>6.1 - Organization's should monitor current risk exposure versus limits on a daily basis.</p>	<p>SCL monitors current risk exposure versus limits on a weekly basis.</p> <p>This practice was noted in the previous assessment report and SCL Management determined that due to limited staffing and because the Pre-Deal Risk Analysis process is done for all term deals, adequate controls were in place. No action to address this was taken.</p>		<p>SCL should consider generating the limit compliance report on a daily basis. Due to the relative low volume of term transactions, it may be sufficient to perform limit compliance checks only on days when term transactions are executed in addition to the current weekly report. This would notify SCL that a position is out of compliance on the day of the transaction rather than waiting until the end of week report, so corrective action may be taken in a timely manner.</p>	<p>Disagree.</p> <p>SCL feels that the low volume nature of the transactions it engages in make weekly reporting the appropriate frequency in light of current staffing resources.</p> <p>However, this functionality may be available with the new ETRM software, in which case SCL does not object to using such available functionality.</p>
<p>6.2 - Risk Reports are distributed to business unit senior management and to the RMC on a regular basis (usually daily, weekly or monthly, as appropriate).</p>	<p>Monthly compliance reports and weekly position and exposure reports are distributed to the ROC, Superintendent, and Mayor and Council staff.</p> <p>However, documentation of sending this information to the designated recipients, particularly the Mayor and City Council staff does not appear to be formally maintained.</p>	 	<p>No recommendation at this time, as this appears to be generally in line with our understanding of Prevalent Practices.</p> <p>SCL should consider formally maintaining evidence of providing the monthly and weekly reports to the Mayor and City Council Staff.</p>	<p>Agreed.</p> <p>Implementation of this recommendation is currently underway.</p>
<p>6.3 - The RMC is informed immediately when an exposure exceeds the approved limit. The committee meets on a same day basis to assess the situation and provide instructions on bringing the</p>	<p>The ROC is notified promptly upon discovery of a limit excession, however since this is monitored on a weekly basis, there may be some lag between when the limit is actually exceeded and</p>		<p>See recommendation in section 6.1 above.</p>	<p>Disagree.</p> <p>SCL feels that the low volume nature of the transactions it engages in make weekly reporting the appropriate frequency</p>

Prevalent Practice	SCL's Current Practice	Categorization	Recommendation	Management Response
position into compliance. They also monitor the execution of the instructions to bring the exposure back within limits.	when it is discovered. In the case that a limit is exceeded, the ROC will receive written notification of the limit excession including a description of the corrective actions planned to bring exposures back within approved limits. The Chair of the ROC must then provide the Superintendent with a written description of the violation.			in light of current staffing resources.
7.				
7.1 - Management reports represent the primary communication statements used by an organization to convey aggregated (i.e., consolidated) commodity risk exposures and business unit performance to executive management and the RMC. A meaningful package of management reports will summarize portfolio positions, market and credit exposures against limits, financial performance, and probabilistic risk measurement.	The ROD produces a weekly status report which is distributed to the ROC, Superintendent, and Mayor and Council staff. This Risk Oversight Council Weekly Status Report includes descriptions of the following: - Market and credit exposures against limits - 5% Tail Risk metric - Performance against the Hedge Plan - Forward position information - Credit exposures. There appears to be limited reporting related to financial performance.		SCL could consider developing additional management reports such as: • Realized Profit & Loss • Unrealized Profit & Loss Additional financial reports would provide additional decision support for front office management as well as provide better clarity to actual performance of the transacting strategies in which SCL is participating.	Agreed. The Risk Report is only one component of the overall monthly financial report delivered to the parties noted. The remainder of the package does contain information about overall financial results including wholesale energy sales. SCL will evaluate the potential benefit of such additional reporting.
7.2 - Organization's have user-friendly reports that present risk information in a consistent manner regardless of functional alignment and position level (e.g., Vice President, Director, Manager, Analyst, etc.) to enable sound decision-making.	Risk information is consistently reported in a user-friendly, high level format that highlights whether risk limits were breached. Detailed information can be provided, but is not reported in the regular reports.		SCL should provide additional detail in the Risk Reports that show not only whether a risk limit was breached, but also whether those limits are being approached and how close to the various limits the organization is.	Agreed. SCL will evaluate the potential benefit of such reporting.
7.3 - Management reports are typically generated and prepared by a control function independent of front office influence (e.g., risk management or risk control).	The ROD generates the risk reports for Management. ROD is independent from front office.		No recommendation at this time, as this appears to be generally in line with our understanding of Prevalent Practices.	
7.4 - Organizations ensure management reporting is independently performed to ensure objectivity and accuracy and to prevent manipulation or fraud.	The ROD is independent from the transacting function of SCL, and is responsible for preparing management reports. The ROD depends on generation position forecasts that are developed by the PMD. Both the ROD and Finance division validate that the position information is accurately uploaded into		SCL may consider realigning certain responsibilities related to providing generation position information for management reporting to allow for independent management reports. SCL may also consider developing model validation procedures to be performed by an independent function prior to inclusion of the position information in the Cash	Agreed. The process is currently underway to fill two vacant positions within the Risk Oversight Division. The skills being sought will greatly strengthen the ROD in this area.

Prevalent Practice	SCL's Current Practice	Categorization	Recommendation	Management Response
	<p>the Cash from Operations Model, which is the tool used to generate the risk compliance reports. However, there does not appear to be independent evaluation or validation of the front office generated positions.</p> <p>This was noted in the previous report and SCL noted at that time that they felt that their current process provided reasonable control over the forecasting numbers / output and that moving this responsibility would require increases in staffing and budget. No action was taken.</p>		from Operations Model.	
<p>7.5 - Organizations provide executive management and the RMC with reports that are generated from read- and write-protected data, time-stamped, and independently certified.</p>	<p>SCL management reports are generated from protected and secured data. Data from the Cash from Operations Model is stored on a restricted server and is saved in a read-only format. All management reports are sent out in PDF format.</p>		<p>No recommendation at this time, as this appears to be generally in line with our understanding of Prevalent Practices.</p>	
<p>7.6 - Types of reports prepared for the RMC, executive and line management vary based on the organization's risk profile. At a minimum, energy companies with commodity transacting operations prepare the following report types:</p> <ul style="list-style-type: none"> - Position - At-risk measures - Exposure versus limits - Limit compliance - Stress testing - Credit exposure 	<p>The reports prepared for the ROC, Superintendent, and Mayor and Council staff contain the following items:</p> <ul style="list-style-type: none"> - Position - Risk metrics - Exposure versus limits - Limit Compliance - Credit exposure <p>Financial performance and stress testing are not included. In addition, there appears to be very limited management reporting that is shared with line management.</p>		<p>SCL could consider including additional financial performance and stress testing information to its reports for the ROC.</p> <p>This could be done on a periodic basis (such as once per quarter) so that the ROC can understand what types of events that might cause movements to revenue and profitability.</p>	<p>Agreed.</p> <p>Financial performance is included in the monthly Financial Report. Stress testing of cash from operations was reported on during 2010, but with the establishment of the Rate Stabilization Account, the utility is no longer directly exposed to this volatility.</p> <p>SCL will evaluate the potential benefit of such additional reporting.</p>
8.				
<p>8.1 - Organizations require signatures of acceptance from employees.</p>	<p>The RMP includes a compliance statement which employees must sign to acknowledge compliance with the RMP.</p> <p>The Procedures Manual describes the requirement of annual training for front, middle, and back offices to review the RMP and Procedures Manual in addition to SCL's IRP and regulatory updates.</p>		<p>No recommendation at this time, as this appears to be generally in line with our understanding of Prevalent Practices.</p>	

B. Transactional Controls

Transacting processes are generally considered a systematic set of operational steps related to transacting in the energy markets. Typically, these operational steps are collectively referred to as the transactional lifecycle, which begins with the origination of an energy transaction and ends with final recording into the organization’s accounting books and records.

Corresponding controls are usually designed to help maintain transactional integrity and consistency with an organization’s stated risk tolerances and authorized activities. An ineffective transactional control structure may increase the likelihood for an organization to experience undesirable outcomes which may include fraudulent behavior, data corruption, unenforceable contracts, and regulatory investigations (e.g., Federal Energy Regulatory Commission (FERC) intervention).

Transaction processing controls include the following control components:

1. Pre-Deal Process
2. Deal Execution
3. Deal Capture and Amendment
4. Deal Validation
5. Contract Administration
6. Confirmations
7. Settlement
8. Scheduling & Nomination

SCL’s current operational processes were assessed relative to each control component, against industry prevalent practices and the corresponding findings and recommendations are presented below.

Prevalent Practice	SCL’s Current Practice	Categorization	Recommendation	Management Response
1.				
1.1 - The pre-deal process consists of the preliminary steps performed by transacting personnel to formulate trading strategies and define action triggers to execute those strategies.	SCL’s PMD is responsible for initiating all pre-deal term, prompt month, balance of the month, day ahead and real time analysis for electrical energy transacting. Periodic meetings are held to discuss trading strategies and activities. Hedging plans and strategies are created and reviewed / approved and	✓	No recommendation at this time, as this appears to be generally in line with our understanding of Prevalent Practices.	

Prevalent Practice	SCL's Current Practice	Categorization	Recommendation	Management Response
	executed against throughout the year.			
1.2 - The pre-deal process typically begins with a planning meeting attended by transacting personnel on a <i>daily</i> basis.	SCL's pre-deal process consists of a daily set of instructions for the Real Time and Day-Ahead desks & the completion of a Pre-Deal Risk Assessment Form for any transaction with a term of 7 days or longer. Due to the low number of daily transactions, planning meetings are scheduled on a weekly basis with ad hoc discussions held daily and/or on an as-needed basis.	✓	No recommendation at this time, as this appears to be generally in line with our understanding of Prevalent Practices.	
1.3 - Trading strategies and schemes are proposed consistent with the organization's business and operational objectives and senior management's approved and communicated risk tolerances.	SCL adheres to a conservative long-term planning / hedging schedule. The utility is long a significant amount of power and given this surplus in nearly each month, the predominant activity of SCL in the near term markets is to sell this excess power as the certainty of the amount of surplus improves. Hedging plans and strategies are created and reviewed / approved and executed against throughout the year. Pre-Deal Risk Assessment forms are required for all transactions with a term of seven days or longer. Traders are required to select from a menu of transaction types that match the authorized product list in the WERM. All Pre-Deal Risk Assessment forms are also required to be acknowledged by a Power Marketing supervisor or manager and reviewed by the Risk Oversight Division.	✓	No recommendation at this time, as this appears to be generally in line with our understanding of Prevalent Practices.	
1.4 - Organizations use the pre-deal process as an opportunity to initiate front office discussions on new trading products and assess the existing infrastructure's capabilities to effectively manage product risks.	Transactions executed based on the Pre-Deal Risk Assessment forms are regularly scheduled for discussion during the ROC weekly meetings. During the ROC weekly meetings, a standing agenda item is to provide a market update & position discussion along with a recap and discussion of any risk limit violations that occurred since the last meeting.	✓	No recommendation at this time, as this appears to be generally in line with our understanding of Prevalent Practices.	
2.				
2.1 - If a deal is executed off-premise (i.e., off the Trading Floor), controls must provide	Per Policy, no SCL transactions are permitted to be executed off-premises. Power Marketers are required to call	✓	No recommendation at this time, as this appears to be generally in line with our	

Prevalent Practice	SCL's Current Practice	Categorization	Recommendation	Management Response
the means to ensure the deal is documented, captured, and confirmed within the organization's existing transacting technology systems and control infrastructure.	counterparties on a recorded line when transacting standard and non-standard purchases and sales or transacted on the ICE electronic trading platform which has an automated deal capture data retention service.		understanding of Prevalent Practices.	
2.2 - Organizations impose policies that limit transacting activities to the organization's "official" place of business.	The WERM Policy expressly limits transacting activities to SCL offices.	✓	No recommendation at this time, as this appears to be generally in line with our understanding of Prevalent Practices.	
2.3 - Organizations ensure traders/marketers conduct business and make trading decisions in a manner consistent with the organization's existing risk infrastructure. These include compliance with respect to writing deal tickets, checking counterparty creditworthiness and limits, and recording phone conversations.	<p>The policies and procedures governing transacting in the physical wholesale energy markets varies by strategy & transacting type.</p> <p>Unstructured Transactions: deal executions are covered by the WERM Policy and Procedures Manual.</p> <p>Structured Transactions / Requests For Proposals ("RFP"): deal executions are covered by the WERM Policy and Procedures Manual.</p> <p>Renewable Energy Credit Transactions: deal executions are not covered by the WERM Policy. SCL has developed a separate document which establishes policies & procedures governing REC and Carbon transactions.</p>	👉	<p>The WERM Policy describes the process of obtaining approval for both unstructured and structured transactions. It also describes the RFP process for structured transactions. It should be updated with the policies and procedures pertaining specifically to REC and Carbon transactions.</p> <p>SCL should continue to implement their new trading system so that it will become the system of record and assist in the control of deal capture information for unstructured and structured transaction and new products such as REC's and Carbon products. A centralized database would improve data measurement and management throughout the transaction lifecycle, minimize errors and reduce lost data, as well as streamline data requests for both internal and external reporting and assessments.</p>	<p>Agreed.</p> <p>SCL will develop an internal work plan for incorporating the recommendations that relate to the Procedures Manual. This work plan will establish responsibility for completion, an expected timeline, and a mechanism for tracking progress towards that goal. Revisions to the Procedure Manual will be subject to final approval by the ROC to become effective.</p> <p>Robust testing of the new TRM system is currently underway.</p> <p>SCL will evaluate the potential benefits of such enhanced reporting.</p>
2.4 - The Front Office executes energy transactions in a manner consistent with approved procedures.	<p>The PMD executes transactions in a manner consistent with stated policies and procedures. However, some of these documented procedures (such as front-office generating confirmations) are not in alignment with prevalent practices and are discussed in more detail later in this document.</p> <p>Additionally, while ICE is an acknowledged trading platform for executing transactions, this is not adequately documented in the Procedures Manual or the RMP.</p>	📄	SCL should update the Procedures Manual and the RMP to specifically state that trading using electronic trading platforms, specifically ICE, is an allowable mode of transacting and one that would not require recordings via phone lines since the electronic trading platform has its own deal capture recording capabilities via the agreements between the counterparties.	<p>Agreed.</p> <p>SCL will address this by incorporating the recommendations into the next set of proposed changes to the RPM. Per the policy, any proposed changes to the Risk Management Policy put forth by SCL are subject to approval by the Council.</p> <p>SCL will develop an internal work plan for incorporating the recommendations that relate to the Procedures Manual. This work plan will establish responsibility for completion, an expected timeline, and a mechanism for tracking progress towards that goal. Revisions to the Procedure Manual will be subject to final approval by the ROC to become effective.</p>
2.5 – The Front Office hedges market exposure associated with core business strategies.	The PMD hedges market exposure through a combination of real time, day ahead, balance of the month, prompt month, and long term transactions up	✓	No recommendation at this time, as this appears to be generally in line with our understanding of Prevalent Practices.	

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	to 24-months and beyond. (Policy has recently been extended to 24 months from the previously allowed 18 months.)			
2.6 – The Front Office transacts with approved counterparties within established credit limits.	<p>The PMD transacts with approved and active counterparties by monitoring the Credit Window Report from Power Ops & receiving the Credit Exposure Report, which is distributed daily to the Power Marketers.</p> <p>The scheduling / deal capture application, Power Ops, has functionality to restrict users from selecting counterparties that have exceeded established credit limits but it can be overridden by the person entering the transaction.</p> <p>The counterparty available credit field which appears on the deal ticket is not being calculated properly and cannot be relied upon for accuracy.</p>		<p>SCL should consider updating procedures and information systems to improve the identification of accepted counterparties prior to executing transactions.</p> <p>SCL should also integrate the credit risk management / monitoring activities with the transacting activities in an enterprise-wide deal capture application.</p> <p>SCL should consider implementing some type of exception report or notification functionality in the system to inform Credit and/or the ROD when traders have overridden the credit exceedances warning.</p> <p>SCL also needs to correct the problem of within Power Ops related to displaying incorrect counterparty credit available on the deal ticket produced from the system. This may be something that is corrected once the new system is implemented, but this needs to be an area of focus so that transactions are not inadvertently executed with a company that is approaching or above their established credit threshold.</p>	<p>Agreed.</p> <p>SCL will develop an internal work plan for incorporating the recommendations that relate to the Procedures Manual. This work plan will establish responsibility for completion, an expected timeline, and a mechanism for tracking progress towards that goal. Revisions to the Procedure Manual will be subject to final approval by the ROC to become effective.</p> <p>Robust testing of the new TRM system is currently underway.</p> <p>SCL will evaluate the potential benefits of such enhanced reporting.</p>
2.7 – The Front Office works with the Middle Office to ensure that transactions are recorded correctly and valuation and risk measurement are performed according to the RMC's approved methodologies.	The PMD enters all transactions into Power Ops each day and the ROD verifies these transactions daily using the Trade Recap Report. The analytical support behind the risk metric calculation is provided by the SCL Finance Department.		SCL should consider updating the WERM to include reports that measure SCL's physical energy position and risk exposure in discrete time intervals. Establishing a proper book structure could help to identify weaknesses and opportunities for enhancement in the control environment.	<p>Agreed.</p> <p>SCL will evaluate the potential benefit of such reporting.</p>
3.				
3.1 - Organizations align the responsibility of deal capture with the front office.	SCL aligns the responsibility of deal capture with the PMD.		No recommendation at this time, as this appears to be generally in line with our understanding of Prevalent Practices.	
3.2 - The Front Office ensures transaction terms are completely documented and accurately recorded in a <i>centralized</i> trading and risk management system by the close of the business day.	<p>The official source of data for SCL power marketing activities reside within the scheduling / deal capture application, Power Ops.</p> <p>The SCL PMD has accumulated several MS Excel workbooks, MS Access databases, SYBASE queries and reports to determine transactions are captured. The deal capture process for structured transactions at</p>		<p>SCL should continue to implement their new trading system so that it will become the system of record.</p> <p>A centralized system could improve data measurement and management throughout the transaction lifecycle, minimize errors and reduce lost data, as well as streamline data requests for both internal and external reporting and assessments.</p>	<p>Agreed.</p> <p>Robust testing of the new TRM system is currently underway.</p> <p>SCL will evaluate the potential benefits of such enhanced reporting.</p> <p>SCL will develop an internal work plan for incorporating the recommendations that relate to the Procedures Manual. This work plan will establish responsibility for</p>

Prevalent Practice	SCL's Current Practice	Categorization	Recommendation	Management Response
	<p>times is delayed due to the complexity of capturing the different attributes of these non-standard deals.</p> <p>SCL is implementing a trading and risk management system which is intended to be the centralized system of record for all wholesale transacting activities. This system is currently partially implemented as transactions are being executed in the new system. However, not all functionality is currently operational. The transacting system, once fully implemented, will have bi-directional communication with Power Ops to allow for all transactions to be contained in the trading system.</p> <p>SCL currently transacts locations (NW & SW) that are not specifically defined in the WERM Policy.</p> <p>SCL currently transacts certain deal types (Transmission) that are input into the system of record without identifying a specific HUB.</p> <p>SCL currently defines transaction types (RECs) in the WERM policy that are not available for selection in the system of record.</p>		<p>In addition, SCL should also establish guidelines to consistently capture the designated accounting treatment at deal entry. Given the recent updates to accounting standards and the interpretation of those standards, along with the potential for increasing complexity of SCL's transacting profile (potential usage of options), SCL should consider a training session to refresh derivative accounting capabilities to help refine the derivative accounting process and future system requirements.</p> <p>SCL should align locations, transaction types, etc., found in the WERM Policy to the selections that are made available via "drop-down" menus in the new ETRM system of record.</p> <p>SCL should consider restricting tenor, transaction type, etc., by Trader ID and/or Book Classification.</p> <p>SCL should also consider building "sanity checks" into the new ETRM system of record to prevent entry of unreasonable volumes, prices, etc.</p>	<p>completion, an expected timeline, and a mechanism for tracking progress towards that goal. Revisions to the Procedure Manual will be subject to final approval by the ROC to become effective.</p>
<p>3.3 - The deal ticket itself is a key control mechanism and prevailing practices include sequential pre-numbering, deal ticket tracking and logging, secured access, and electronic archiving.</p>	<p>SCL has a deal ticket process established. Current deal tickets are not generated unless specified by the Power Ops user. At the time a transaction is entered into Power Ops, the user has to create a deal ticket through the offer editor screen. Once the offer editor menu button is selected, Power Ops will generate a deal ticket. Users have the ability to retrieve archived deal tickets and selected users can print.</p> <p>SCL's WERM Policy and Procedures Manual documents how to create deal tickets but not how to edit, track changes, or investigate / explain / resolve deal ticket discrepancies.</p> <p>Certain fields displayed on SCL deal tickets (specifically counterparty credit available) use calculated information which is known to be incorrect.</p> <p>SCL is in the process of implementing</p>		<p>Refer to 3.2 above for comments on the benefits of a centralized system.</p> <p>SCL should consider updating procedures and information systems to improve the creation, identification and revision of deal tickets.</p> <p>In the near-term, SCL should address the problem of incorrect calculated information being displayed on the deal tickets.</p> <p>Longer term, SCL should test the functionality in the new system to make sure that information (such as credit exposure) that is relied upon by transacting and risk personnel is complete and accurate.</p>	<p>Agreed.</p> <p>Robust testing of the new TRM system is currently underway.</p> <p>SCL will evaluate the potential benefits of such enhanced reporting.</p> <p>SCL will develop an internal work plan for incorporating the recommendations that relate to the Procedures Manual. This work plan will establish responsibility for completion, an expected timeline, and a mechanism for tracking progress towards that goal. Revisions to the Procedure Manual will be subject to final approval by the ROC to become effective.</p>

Prevalent Practice	SCL's Current Practice	Categorization	Recommendation	Management Response
	<p>an ETRM system, which includes deal capture functionality, but it has not yet been fully implemented.</p>			
<p>3.4 - Deal capture practices require Front Office personnel to model, decompose, and capture embedded options in the transacting system.</p>	<p>Embedded options should be identified in structured transactions through the RFP review process.</p> <p>Our understanding is that there are limited amounts of embedded optionality in the transactions that SCL conducts, and much of this optionality is not of the type that can be commercially exercised.</p>		<p>SCL's ROD should consider developing a common understanding of deal composition concepts and requirements for transactions with embedded options.</p> <p>To the extent that the long-term transactions (such as generation, hydro, wind, etc) contain embedded options, these options should be noted and valued to the extent possible.</p> <p>In addition, stakeholders from ROD should be involved from the beginning of the RFP process through deal validation to ongoing deal monitoring and be educated regarding how to dis-aggregate embedded options and value these.</p>	<p>Agreed.</p> <p>SCL will develop an internal work plan for incorporating the recommendations that relate to the Procedures Manual. This work plan will establish responsibility for completion, an expected timeline, and a mechanism for tracking progress towards that goal. Revisions to the Procedure Manual will be subject to final approval by the ROC to become effective.</p>
<p>3.5 - If deal amendments occur, a formal deal amendment process is clearly established and documented.</p>	<p>Based upon conversations, transactions are currently revised manually and recorded on the existing deal ticket.</p> <p>Previously, a deal ticket correction request form, designed in MS Excel was completed by the PMD, and then emailed to the Settlements group with instructions on the item(s) to revise. The Settlement group maintained a log of all transactions revised, and provides the ROD with access to the log of changes made.</p> <p>Currently, deal amendments are identified, corrected, and monitored primarily by the Settlements group.</p> <p>SCL is in the process of implementing an ETRM system, which includes improved deal capture functionality (which includes a more robust deal amendment process), but it has not yet been fully implemented.</p>		<p>Refer to 3.2 above for comments on the benefits of a centralized system.</p> <p>Once the system is implemented, SCL should update the processes and procedures to document the current practices of deal amendments.</p>	<p>Agreed.</p> <p>Robust testing of the new TRM system is currently underway.</p> <p>SCL will evaluate the potential benefits of such enhanced reporting.</p> <p>SCL will develop an internal work plan for incorporating the recommendations that relate to the Procedures Manual. This work plan will establish responsibility for completion, an expected timeline, and a mechanism for tracking progress towards that goal. Revisions to the Procedure Manual will be subject to final approval by the ROC to become effective.</p>
<p>3.6 - Deal capture practices include Middle or Back Office approval, a system "lock-down" feature for prior business day transactions; and daily audit reports (i.e., Trade Change Report) for monitoring and tracking purposes.</p>	<p>Before entering into term, prompt month, or balance of the month (with a tenor greater than seven days) transactions, the Power Marketers are required to submit a Pre-Deal Risk Assessment form and obtain approval from a Power Marketing Supervisor / Manager and approval from the ROD.</p> <p>The ROD prepares a Trade Recap</p>		<p>Refer to 3.2 above for comments on the benefits of a centralized system.</p> <p>SCL should develop daily audit reports of changes made to deals that have already been captured by the system of record.</p>	<p>Agreed.</p> <p>Robust testing of the new TRM system is currently underway.</p> <p>SCL will evaluate the potential benefits of such enhanced reporting.</p>

Prevalent Practice	SCL's Current Practice	Categorization	Recommendation	Management Response
	<p>Report for the Day Ahead and Balance of the Month transactions executed on a daily basis.</p> <p>The Power Ops application has the functionality to "lock-down" or protect the transactions. Transactions cannot be edited by the PMD beginning 24 hours after the transaction was entered.</p> <p>However, there does not appear to be a trade change report that is generated and/or monitored on a regular basis.</p> <p>SCL is in the process of implementing an ETRM system, which includes improved deal capture functionality (including lock-down capabilities and daily audit reports), but it has not yet been fully implemented.</p>			
<p>3.7 - Off premise transacting is allowed, however procedures and guidelines for conducting off-premise transactions are explicitly documented in the Risk Management Policy. Off-premise transactions, subject to the Company's market, credit and counterparty limits, must be called in, captured on a recorded phone line, and entered into the book of record within 24 hours. A process is in place to determine that off-premise transactions are entered into the system in a timely and accurate manner.</p>	<p>Off-premise trading was not executed during the period May 1, 2009 – April 30, 2011.</p> <p>Off-premise transacting is not allowed per the WERM Policy.</p>		<p>Not Applicable.</p>	
<p>3.8 - Transactions are executed over taped phone lines and are subject to periodic compliance testing by Internal Audit. Recordings are digital and the system is maintained by IT. Transacting personnel can access tapes as necessary but do not have authority to delete recordings. The recording system has search capability for archived records in order to facilitate timely retrieval of specific transactions.</p>	<p>With the exception of deals executed via electronic trading platforms (primarily ICE), all transactions are executed over recorded phone lines. ROD has ownership of this responsibility. Disputed transactions are able to be retrieved and reviewed as necessary.</p> <p>The process and procedures for retrieving information from the phone recordings is documented in the Procedures Manual.</p> <p>Currently, there is not an Internal Audit department within SCL that can perform these types of compliance tests.</p>		<p>SCL should consider having a formal independent review and assessment of the taped phone lines on a pre-determined periodic basis. This could be performed by an Internal Audit function or some other compliance related functional area.</p>	<p>Agreed</p> <p>Staffing limitations and existing vacancies have led to less than optimal segregation of duties. Efforts are underway to fill vacancies within the Risk Oversight Division and once complete, SCL will re-evaluate the distribution of workload to address any shortcomings identified.</p>

Prevalent Practice	SCL's Current Practice	Categorization	Recommendation	Management Response
<p>3.9 - At a minimum, organizations should retain the past 90 days of taped phone conversations, but this time frame may need to be expanded depending on the volume and term of instruments transacted. Conversations are recorded digitally, time-stamped, identifiable by the recording system, and available for review in real-time. A group independent of the front office should perform periodic checks of system functionality.</p>	<p>Currently, SCL is storing all recordings with the ROD. Per the Procedures Manual, all tapes are maintained for 5 years.</p> <p>Previously, the ROD group reviewed samples of selected executed transactions monthly to determine the device was working properly.</p> <p>After the ROD employee that was performing this activity, left SCL, the activity was performed by an IT employee. After the IT employee, that was performing this activity, left SCL, the activity has not been performed by anyone on a regular basis. It is performed by the Settlements group only if there is a counterparty discrepancy.</p>		<p>SCL should designate a group/employee to be responsible for reviewing recorded phone line conversations, at least monthly, to verify that the system is working properly.</p>	<p>Agreed.</p> <p>Staffing limitations and existing vacancies have led to less than optimal segregation of duties. Efforts are underway to fill vacancies within the Risk Oversight Division and once complete, SCL will re-evaluate the distribution of workload to address any shortcomings identified.</p>
4.				
<p>4.1 - Deal entry validation is the end of day "check-out" process to ensure transactions are entered into the transacting systems in a complete, accurate and timely manner. As a prevalent practice, front office deal tickets and transaction summary reports ("Daily Trade Summaries") are independently reconciled by the Middle or Back Office prior to sending confirmations.</p>	<p>There are at least two deal entry validation process performed at SCL on a daily basis.</p> <p>The ROD prepares and prints a Trade Recap Report from MS Access at the end of each trading day, which displays (by trader) all term, day ahead, balance of the month and prompt month transactions executed. The ROD will request the Power Marketer to sign the Trade Recap Report for their transactions executed. This process is duplicated by the Power Marketing group, which prepares a Transaction Summary Report, at the end of each day that a transaction is entered into.</p>		<p>SCL should consider implementing a uniform validation process. This would include accounting for deal tickets and Pre-Deal Risk Assessment Sheets, locating missing deal tickets and Pre-Deal Risk Assessment Sheets and determining that terms are correctly entered into the deal capture system. The Power Marketers could review, compare and accept deal summary reports from the deal capture system.</p>	<p>Agreed.</p> <p>Staffing limitations and existing vacancies have led to less than optimal segregation of duties. Efforts are underway to fill vacancies within the Risk Oversight Division and once complete, SCL will re-evaluate the distribution of workload to address any shortcomings identified.</p>
<p>4.2 - Trader/Marketer sign-off is required on "Daily Trade Summaries" to ensure front office accountability.</p>	<p>The ROD prepares and prints a Trade Recap Report from MS Access at the end of each trading day, which displays (by trader) all term, day ahead, balance of the month and prompt month transactions executed.</p> <p>The ROD requests that the Power Marketer to sign the Trade Recap Report for their transactions executed.</p>		<p>No recommendation at this time, as this appears to be generally in line with our understanding of Prevalent Practices.</p>	

Prevalent Practice	SCL's Current Practice	Categorization	Recommendation	Management Response
4.3 - The Middle or Back Office investigate trade discrepancies with traders directly and resolve immediately.	<p>The SCL ROD investigates trade discrepancies between the City of Seattle confirmations and counterparty confirmations.</p> <p>The ROD - Settlement group - works with the Power Marketers to resolve settlement related discrepancies. This process is dependent upon a host of manual processes, MS Excel workbooks & MS Access databases to organize data.</p>		<p>SCL should consider reducing the manual processes required to identify, investigate and reconcile data.</p> <p>A centralized data system could improve data measurement and management throughout the transaction lifecycle, minimize errors and reduce lost data, as well as streamline data requests for both internal and external reporting and assessments.</p>	<p>Agreed. Robust testing of the new TRM system is currently underway.</p>
4.4 - Trade Tickets/Blotters, Daily Trade Summaries (with sign-off), and exceptions and corresponding resolutions are archived in an organized manner.	SCL ROD is able to retain and retrieve trade tickets, Pre-Deal Risk Assessments forms and Trade Recap Reports.		No recommendation at this time, as this appears to be generally in line with our understanding of Prevalent Practices.	
4.5 - Organizations maintain an "audit trail" of transactions, which enables management to review and validate changes to the "official" book of record.	<p>The "official" system of record, Power Ops, has limited ability to capture the reasons for deal revisions.</p> <p>SCL is dependent on manual processes and supplemental reports from SYBASE, MS Excel and MS Access to track changes and record revisions to transactions.</p> <p>SCL is in the process of implementing an ETRM system, which includes improved deal capture functionality, but it has not yet been fully implemented.</p>		SCL should continue implementing the new electronic deal capture system and test the system to make sure it has the functionality to automatically provide an audit trail for compliance, control and accountability for risk management requirements.	<p>Agreed. Robust testing of the new TRM system is currently underway.</p>
5.				
5.1 - Front, Middle and Back Office responsibilities are segregated to ensure minimizing violations and maximizing the operational integrity of processing transactions, confirmations and settlements. An independent function initiates, follows-up and manages counterparty confirmations. The Legal department is actively involved in reviewing contract clauses and provisions, particularly for non-standard contracts.	The SCL Power Marketers have the necessary access to generate confirmations and are currently performing this task. All confirmations, for transactions with a tenor of longer than 7 days but less than 24 months, are generated by the PMD, after they are sent to the ROD for review and approval. The City Council of Seattle must approve all contracts with terms 24 months and longer after these contracts have been reviewed by the SCL Wholesale Contracts group.		<p>The ROC should consider further refining organizational roles and responsibilities that explicitly define segregation of duties among the PMD, the ROD, and Wholesale Contracts Division.</p> <p>To determine valid enabling agreements and contracts are in place prior to committing to deals and determining that terms of the contract are met throughout the life, a single department should be responsible for processing all contracts and coordinating negotiations with counterparties.</p>	<p>Agreed. Staffing limitations and existing vacancies have led to less than optimal segregation of duties. Efforts are underway to fill vacancies within the Risk Oversight Division and once complete, SCL will re-evaluate the distribution of workload to address any shortcomings identified.</p>
5.2 - A designated person, independent of Front Office, obtains and compiles all counterparty information in a centralized database. As counterparty contact information changes, the database is	The ROD is the official holder of counterparty contact information. It is responsible for updating changes to counterparty information without adjusting historical records so that		No recommendation at this time, as this appears to be generally in line with our understanding of Prevalent Practices.	

Prevalent Practice	SCL's Current Practice	Categorization	Recommendation	Management Response
updated in a timely manner.	audit trails are preserved. SCL currently links to counterparty contact information via the NERC counterparty database to determine that proper names, addresses, etc., are used consistently by the various city divisions. Any changes formally submitted to NERC are programmed to automatically flow directly into Power Ops.			
5.3 - The status of deals in the confirmation process is actively tracked in the book of record. Reports detailing the status of confirmations are generated and reviewed on a daily basis. Confirmations are sent out in a timely manner and are monitored to ensure counterparty receipt, signature and return.	The SCL Power Marketers are responsible for delivering confirmations to the ROD within one business day of executing the transaction. The ROD Analyst tracks status of confirmations in a spreadsheet that is separate from the official system of record.		Refer to 5.1 above for comments on refining roles and responsibilities. Once the new ETRM system is fully implemented, SCL should make sure that it has the functionality of tracking confirmation status enabled.	Agreed. Staffing limitations and existing vacancies have led to less than optimal segregation of duties. Efforts are underway to fill vacancies within the Risk Oversight Division and once complete, SCL will re-evaluate the distribution of workload to address any shortcomings identified.
5.4 – Incoming / Outgoing confirmations are verified against the deal terms in the book of record with minimal manual intervention (i.e. the system has Rightfax or email capabilities). For non-standard deals, the transactor reviews the transaction confirmations/contracts. The transactor is familiar with standard templates. Transaction confirmation documents are retained in electronic form (scanned and cataloged) for a time frame in accordance with guidelines established by the Legal department and/or the Corporate Risk Management Policy.	All confirmations, for transactions with a tenor longer than 7 days but less than 24 months, are generated by the PMD, after which they are sent to the ROD for review and approval. The SCL Power Marketers currently generate confirmations from a template created and maintained in MS Excel (Premonth.xls & MRK.xls). Attributes from each transaction are manually entered in the MS Excel workbook and a series of macros enable the creation of official confirmations. Power Ops or the SYBASE tool developed does not have the functionality to generate confirmations. SCL is in the process of implementing a new ETRM system, which includes automated confirmation generation functionality, but it has not yet been fully implemented.		SCL should consider updating procedures and information systems for sending a written deal confirmation to any involved third party to verify agreements with terms. Ideally, for deals beyond day-ahead transactions, the middle office should electronically generate a standard confirmation from the deal capture system of record.	Agreed. SCL will evaluate the timeframe to full TRM implementation and determine the cost/benefit of correcting this deficiency prior to retirement of the current system.
5.5 - Confirmation discrepancies are investigated independently of the Front Office and are reconfirmed if necessary. As necessary, subject matter or transaction experts are consulted to resolve discrepancies (e.g., Front Office, Legal, Credit). If necessary, phone tapes are pulled to resolve the dispute. Discrepancies are logged and reported for error-prone individuals and/or counterparties.	The SCL ROD investigates trade discrepancies between the City of Seattle confirmations and counterparty confirmations. The process includes listening to transactions recorded on the SCL phone lines, if necessary.		A formal, documented process should set out how items are investigated, explained, and resolved for the confirmation process. SCL could consider reducing the manual processes required to identify, investigate and reconcile data. A centralized data system could improve data measurement and management throughout the transaction lifecycle,	Agreed. SCL will develop an internal work plan for incorporating the recommendations that relate to the Procedures Manual. This work plan will establish responsibility for completion, an expected timeline, and a mechanism for tracking progress towards that goal. Revisions to the Procedure Manual will be subject to final approval by

Prevalent Practice	SCL's Current Practice	Categorization	Recommendation	Management Response
			minimize errors and reduce lost data, as well as streamline data requests for both internal and external reporting and assessments.	the ROC to become effective
6.				
6.1 - Whenever trading transactions are agreed upon, a confirmation is sent to the counterparty as follow up to the verbal trade agreement.	The SCL Power Marketers currently generate all confirmations from a template created and maintained in MS Excel (Premonth.xls & MRK.xls). Attributes from each transaction are manually entered in the MS Excel workbook and a series of macros enable the creation of official confirmations. Power Ops or the SYBASE tool developed does not have the functionality to generate confirmations. SCL is in the process of implementing an ETRM system, which includes automated confirmation generation functionality, but it has not yet been fully implemented.		SCL should consider establishing a sound internal control environment with a separation of duties between a transaction's execution and the generation of the confirmation. To establish the proper segregation of duties and maintain a sound control infrastructure, the confirmation function should be performed by a group independent from transaction execution.	Agreed Staffing limitations and existing vacancies have led to less than optimal segregation of duties. Efforts are underway to fill vacancies within the Risk Oversight Division and once complete, SCL will re-evaluate the distribution of workload to address any shortcomings identified.
6.2 - A confirmation is the official record of the terms of a transaction sent out by each interested party prior to the actual settlement of the transaction itself.	SCL uses confirmations to verify that transaction attributes are as agreed upon between SCL and the counterparty for wholesale transactions.		No recommendation at this time, as this appears to be generally in line with our understanding of Prevalent Practices.	
6.3 - The confirmation contains the exact details of the transactions and serves as the legal, practical, and anti-fraud vehicle in the event of contract dispute or counterparty default.	When SCL issues confirmations, the following details are provided on the confirming document: - Entities buying or selling; - Address, phone number and fax number of the entities and the individuals responsible for the transaction; - Contract Price, Quantity, Total Quantity, Delivery Point, Delivery Period, Product & Broker; and Transaction Date, Transaction Number and any Special Terms and Exceptions.		No recommendation at this time, as this appears to be generally in line with our understanding of Prevalent Practices.	
6.4 - Although some companies manually generate confirmations, it is considered leading practice to automatically issue a confirmation through the trading and risk	The SCL Power Marketers currently generate all confirmations from a template created and maintained in MS Excel (Premonth.xls & MRK.xls).		In the near-term, SCL should evaluate the current system and determine whether detailed transaction information could be automatically downloaded from PowerOps	Agreed SCL will evaluate the timeframe to full TRM implementation and determine the

Prevalent Practice	SCL's Current Practice	Categorization	Recommendation	Management Response
management system.	<p>Attributes from each transaction are manually entered in the MS Excel workbook and a series of macros enable the creation of official confirmations. Power Ops or the SYBASE tool developed does not have the functionality to generate confirmations.</p> <p>SCL is in the process of implementing an ETRM system, which includes automated confirmation generation functionality, but it has not yet been fully implemented.</p>		<p>into Excel to eliminate the potential errors associated with manually entering information into the MS Excel workbook.</p> <p>SCL should also continue implementation of the new trading and risk management system and should enable the automated confirmation functionality as soon as possible in order to have appropriate segregation of duties.</p>	<p>cost/benefit of correcting this deficiency prior to retirement of the current system.</p> <p>Agreed.</p> <p>Robust testing of the new TRM system is currently underway.</p>
6.5 - The Middle Office is responsible for initiating, following up, and controlling counterparty confirmations.	<p>SCL's Power Marketers have ownership of generating SCL confirmations.</p> <p>SCL's ROD is responsible for confirmation record keeping.</p>		<p>The ROC should consider further refining organizational roles and responsibilities that explicitly define segregation of duties among the PMD, the ROD, and Wholesale Contracts Division.</p>	<p>Agreed.</p> <p>Staffing limitations and existing vacancies have led to less than optimal segregation of duties. Efforts are underway to fill vacancies within the Risk Oversight Division and once complete, SCL will re-evaluate the distribution of workload to address any shortcomings identified.</p>
6.6 - Written outgoing confirmations should be sent to the attention of counterparty's department that is independent of the trading room and require an authorized signature on a returned confirmation as legal support for contract enforceability.	<p>Confirmations generated by SCL are sent to the transacting entity subject to the terms of specific enabling agreements.</p>		<p>No recommendation at this time, as this appears to be generally in line with our understanding of Prevalent Practices.</p>	
6.7 - Written incoming confirmations are compared in detail with the written outgoing confirmations, and any discrepancies are recorded in a discrepancy log, addressed and resolved within a specified period (this period ranges between one to three business days).	<p>The SCL ROD investigates trade discrepancies between the City of Seattle confirmations and counterparty confirmations. The process includes listening to transactions recorded on the SCL phone lines, if necessary.</p>		<p>SCL should expand the confirmation section of the WERM Policy to include a formal, documented process which details how items are investigated, explained, and resolved for the confirmation process. SCL could consider reducing the manual processes required to identify, investigate and reconcile data.</p> <p>SCL is in the process of implementing an ETRM system, which includes automated confirmation generation functionality, but it has not yet been fully implemented.</p>	<p>Agreed.</p> <p>SCL will develop an internal work plan for incorporating the recommendations that relate to the Procedures Manual. This work plan will establish responsibility for completion, an expected timeline, and a mechanism for tracking progress towards that goal. Revisions to the Procedure Manual will be subject to final approval by the ROC to become effective.</p>
6.8 - It is very important that all discrepancies are followed up, and amended signed confirmations are obtained.	<p>The SCL ROD investigates trade discrepancies between the City of Seattle confirmations and counterparty confirmations. The process includes listening to transactions recorded on the SCL phone lines, if necessary.</p>		<p>SCL should consider updating and/or documenting the expectation of senior management when discrepancies occur between SCL and counterparties.</p>	<p>Agreed.</p> <p>SCL will develop an internal work plan for incorporating the recommendations that relate to the Procedures Manual. This work plan will establish responsibility for completion, an expected timeline, and a mechanism for tracking progress towards that goal. Revisions to the Procedure Manual will be subject to final approval by</p>

Prevalent Practice	SCL's Current Practice	Categorization	Recommendation	Management Response
				the ROC to become effective
6.9 - Amended confirmations reflect all, if any, agreed upon changes in the terms of the transaction.	Transactions are currently revised manually and recorded on the existing deal ticket.		SCL should consider updating procedures and information systems to improve the creation, identification and revision of deal tickets. SCL should expand the confirmation section of the WERM Policy to include a formal, documented process which details how items are investigated, explained, and resolved for the confirmation process.	Agreed. SCL will develop an internal work plan for incorporating the recommendations that relate to the Procedures Manual. This work plan will establish responsibility for completion, an expected timeline, and a mechanism for tracking progress towards that goal. Revisions to the Procedure Manual will be subject to final approval by the ROC to become effective The newly implemented TRM, when fully functional, should provide the ability to aggregate transactional detail as recommended.
6.10 - Organizations have installed telephone-recording systems as a secondary means to resolve trade disputes, discrepancies or errors.	SCL has the capability & functionality to monitor phone recordings of PMD activities. With the exception of deals executed via electronic trading platforms, all transactions are executed over recorded phone lines. ROD has ownership of this responsibility. Disputed transactions are able to be retrieved and reviewed as necessary. The process and procedures for retrieving information from the phone recordings is documented in the Procedures Manual.		No recommendation at this time, as this appears to be generally in line with our understanding of Prevalent Practices.	
6.11 - When resolving a trade discrepancy or dispute, the tape is reviewed by an independent party along with the trader.	Discrepancies or disputes between SCL and their counterparties that require the review of taped conversations are conducted by the ROD. The Manager of Risk Control & Settlements will review the taped transaction. There is also the capability to send counterparties the taped conversation, if needed. The Power Marketer involved will be involved if the disputed transaction requires detailed explanation.		No recommendation at this time, as this appears to be generally in line with our understanding of Prevalent Practices.	
7.				
7.1 - Organizational requirements for transaction settlements are typically considered to include the ability to electronically transfer data from the scheduling system directly into the system	There are several MS Excel workbooks prepared throughout the month prior to the settlement of SCL transactions. The four primary		SCL should consider updating procedures and information systems to improve the settlement and electronic transfer of data from scheduling systems to into the system	Agreed. SCL will develop an internal work plan for incorporating the recommendations that relate to the Procedures Manual. This work

Prevalent Practice	SCL's Current Practice	Categorization	Recommendation	Management Response
of record.	<p>workbooks used are:</p> <p>Checkout Sheet – is the primary record for checking out. It records the monthly marketed energy and total dollars according to counterparty.</p> <p>Checkout Workbook – has daily and hourly data transferred from Power Ops in order to aid analysis to prepare the Checkout Sheet.</p> <p>Monthly Power Ops Change Log - provides background and explanations concerning settlement related adjustments made in Power Ops.</p> <p>Checkout Contact Sheet – has settlement contact information for all counterparties.</p> <p>There are also a number of miscellaneous documents and MS Excel workbooks prepared throughout the month.</p>		<p>of record.</p> <p>SCL should also consider building out reports which contain transaction-specific detail that can easily be aggregated up by counterparty, volume, price, etc., instead of the current methodology which presents counterparty totals aggregated by price which is difficult to break down into transaction-specific detail.</p>	<p>plan will establish responsibility for completion, an expected timeline, and a mechanism for tracking progress towards that goal. Revisions to the Procedure Manual will be subject to final approval by the ROC to become effective</p> <p>The newly implemented TRM, when fully functional, should provide the ability to aggregate transactional detail as recommended.</p>
7.2 - Processes are in place to ensure the consistent uploading of data and manual checks are used to make sure rejected data is investigated and researched in a timely manner.	<p>There are several manual processes required to determine data is extracted. A template file located on the SCL network at I:\MidOff\After-the-fact\Checkout_Workbooks\Checkout_Workbook_Template.xls is used to obtain data from Power Ops. This template has to then be renamed, added to the proper year folder and used simultaneously with Power Ops open to transfer (copy + paste) Megawatts & dollar amount into MS Excel.</p>		<p>Refer to 7.1 above for comments updating policies and information systems.</p> <p>Refer to 7.1 above for comments on building out reports.</p>	<p>Agreed.</p> <p>SCL will develop an internal work plan for incorporating the recommendations that relate to the Procedures Manual. This work plan will establish responsibility for completion, an expected timeline, and a mechanism for tracking progress towards that goal. Revisions to the Procedure Manual will be subject to final approval by the ROC to become effective</p> <p>The newly implemented TRM, when fully functional, should provide the ability to aggregate transactional detail as recommended</p>
7.3 - Any items that do not reconcile are promptly investigated in accordance to formal reconciliation procedures.	<p>There are duplicative processes in reconciling data between the ROD and General Accounting. ROD prepares a checklist which is the primary record for checking out, recording and reconciling monthly marketed volumes and settlement prices.</p> <p>The General Accounting group also prepares a separate spreadsheet that is independently reconciled to monthly marketed volumes and settlement prices. Using a combination of Power Ops, a selector in SYBASE (the provision types) and the Financial Information Billing System ("FIBS") and</p>		<p>SCL should identify one department that is responsible for the verification and reconciliation of data from the official system of record.</p> <p>Refer to 7.1 above for comments updating policies and information systems.</p> <p>Refer to 7.1 above for comments on building out reports.</p>	<p>Agreed.</p> <p>SCL will develop an internal work plan for incorporating this recommendation. This work plan will establish responsibility for completion, an expected timeline, and a mechanism for tracking progress towards that goal.</p>

Prevalent Practice	SCL's Current Practice	Categorization	Recommendation	Management Response
	the check-sheet from ROD, the reconciliation process is performed in the format necessary for General Accounting to perform their monthly reconciliation process.			
7.4 - In accordance with contract language, counterparties may be assessed late charges. Actual assessment of charges may vary due to the nature of the counterparty relationship, but are formally tracked and monitored.	SCL will assess charges according to the terms and conditions in the WSP contracts signed with the counterparties.	✓	No recommendation at this time, as this appears to be generally in line with our understanding of Prevalent Practices.	
7.5 - Settlement discrepancies are handled in a timely fashion, in accordance with established guidelines or written procedures.	<p>The ROD – Settlement Analyst will identify and communicate data related to discrepancies (taped or transcripts of phone recording, confirmation, contract, etc) to specific counterparties where they will attempt to resolve the discrepancy.</p> <p>The ROD – Settlement group works with the Power Marketers to resolve settlement related discrepancies. This process is dependent upon a host of manual processes, MS Excel & MS Access to organize data.</p>	✓	No recommendation at this time, as this appears to be generally in line with our understanding of Prevalent Practices.	
7.6 - Any discrepancy in settlement that is more than a routine situation is brought to the attention of the Front Office and a Senior Manager/Supervisor in the Back Office. Further action should be handled and/or directed by management. All discrepancies should be entered into a formal log, which should be reviewed regularly. The log should provide a clear audit trail of the nature of the discrepancy, means of resolution, and final resolution.	<p>Formal authority has been granted by the SCL CFO to allow the Manager of Risk Control & Settlements and any Settlements Analyst the ability to adjust invoice errors that cannot be resolved that are less than or equal to \$200.00 per settlement period.</p> <p>The Procedures document also states that the Settlements Analyst is authorized to make changes to existing transactions not to exceed \$50,000 without additional authorization</p>	✓ 	<p>No recommendation at this time, as this appears to be generally in line with our understanding of Prevalent Practices.</p> <p>SCL should reconsider the authorization limit amount related to the Settlements Analyst making changes to transactions. The \$50,000 limit appears to be excessive when compared to the other levels of risk tolerance that SCL has in place.</p>	<p>Agreed.</p> <p>SCL will develop an internal work plan for incorporating the recommendations that relate to the Procedures Manual. This work plan will establish responsibility for completion, an expected timeline, and a mechanism for tracking progress towards that goal. Revisions to the Procedure Manual will be subject to final approval by the ROC to become effective</p>

C. Credit Risk Management

Credit risk management combines professional judgment and mechanistic techniques to measure, monitor, control, and report counterparty credit exposures associated with commodity transacting activities. A credit risk management program is comprised of policies, processes, controls and systems to mitigate total credit exposure in the event of counterparty default.

Prevalent Practice	SCL's Current Practice	Categorization	Recommendation	Management Response
1.				
1.1 - Credit risk oversight is arguably under the jurisdiction of a RMC.	<p>Credit risk falls under the jurisdiction of the ROC. The CFO, who is also the Chair of the ROC, is responsible for informally setting the overall counterparty credit limit threshold and for recommending to the ROC the methodology used to compute approved credit limits.</p> <p>Outside of the CFO, others in the organization do not have a clear understanding of the process and analysis done in coming up with the overall credit threshold.</p> <p>All credit violations are reported to the ROC, and the ROC is responsible for determining appropriate actions.</p>		SCL should consider formalizing and documenting the process for establishing the overall credit threshold limit for the organization and having documentation for that limit.	<p>Agreed.</p> <p>SCL will develop an internal work plan for incorporating the recommendations that relate to the Procedures Manual. This work plan will establish responsibility for completion, an expected timeline, and a mechanism for tracking progress towards that goal. Revisions to the Procedure Manual will be subject to final approval by the ROC to become effective.</p>
1.2 - Credit oversight and authorization is clearly defined in a formal committee charter that is approved by the RMC.	Credit oversight and authorization is included in the RMP, which has been approved by the RMC.		No recommendation at this time, as this appears to be generally in line with our understanding of Prevalent Practices.	
<p>1.3 - Credit working group responsibilities include:</p> <ul style="list-style-type: none"> - designing and developing a credit risk policy for RMC approval; - ensuring policy compliance; establishing clearly defined roles and responsibilities for credit personnel; - establishing a committee decision-making framework; - periodically assessing current rating methodologies, exposure measurement practices, limit structures, credit risk reports and limit authorities for adequacy; - recommending models and methodologies used for rating counterparties and measuring credit exposure for RMC approval; 	SCL does not have a Credit working group in place. These responsibilities are currently spread across the Credit function, ROD, and the Risk Oversight Director.		SCL may consider creating a Credit working group and delegating these responsibilities to establish a group which could dedicate more time to focus on Credit Risk Management.	<p>Agreed.</p> <p>SCL will evaluate the potential benefit of establishing such a working group.</p>

Prevalent Practice	SCL's Current Practice	Categorization	Recommendation	Management Response
<ul style="list-style-type: none"> - recommending credit limit structures and authorities for RMC approval; and - reviewing exposure reports and recommending corrective action for RMC approval in the event of a credit limit violation and/or counterparty default. 				
2.				
<p>2.1 - Organizations' risk management infrastructure will always include a Credit policy, which memorializes the organization's Credit controls to mitigating the inherent risks associated with commodity transacting activities.</p>	<p>SCL's RMP references the Credit practices of the organization and the Procedures document goes into significantly more detail on credit risk tolerance, credit limit assignment methodology, credit limit change management, monitoring credit exposure, etc.</p> <p>However, some of the documented processes and controls within the Procedures Document do not reflect the procedures currently being performed as described by Credit personnel.</p>		<p>SCL could consider revising the Credit Procedures to reflect processes, procedures and controls as currently performed.</p>	<p>Agreed.</p> <p>SCL will develop an internal work plan for incorporating the recommendations that relate to the Procedures Manual. This work plan will establish responsibility for completion, an expected timeline, and a mechanism for tracking progress towards that goal. Revisions to the Procedure Manual will be subject to final approval by the ROC to become effective.</p>
<p>2.2 - At a minimum, risk policies document the structure, processes, controls, and systems to manage market and credit risk.</p>	<p>See observation noted above in section 2.1.</p>		<p>See recommendation noted above in section 2.1.</p>	<p>Agreed.</p> <p>SCL will develop an internal work plan for incorporating the recommendations that relate to the Procedures Manual. This work plan will establish responsibility for completion, an expected timeline, and a mechanism for tracking progress towards that goal. Revisions to the Procedure Manual will be subject to final approval by the ROC to become effective.</p>
<p>2.3 - Organizations design one comprehensive credit policy to make the maintenance and administration responsibilities more manageable.</p>	<p>Credit Policy and Procedures are documented in the WERM Policy and the WERM Procedures Manual respectively</p>		<p>No recommendation at this time, as this appears to be generally in line with our understanding of Prevalent Practices.</p>	
<p>2.4 - Once a credit policy is approved, all relevant transacting personnel are required to acknowledge in writing that they have been informed of and understand the policies. The policies and amendments should be announced in a timely manner and be readily accessible to each employee by hard or electronic copy. All relevant trading personnel should be required to reaffirm the policies annually.</p>	<p>Credit Policy is documented in the WERM Policy which is required to be acknowledged by employees on an annual basis.</p>		<p>No recommendation at this time, as this appears to be generally in line with our understanding of Prevalent Practices.</p>	

Prevalent Practice	SCL's Current Practice	Categorization	Recommendation	Management Response
<p>2.5 - A comprehensive credit policy should include, at a minimum:</p> <ul style="list-style-type: none"> - A credit risk tolerance statement and policy objectives; - Identification of credit risk exposures (e.g., pre-settlement, settlement, current exposure, potential exposure), sources and mitigation techniques; - Delegated credit authorities and approvals, including clearly defined credit personnel roles and responsibilities, reporting lines and an illustration of the credit organization structure; - the credit risk assessment methodology including scoring models, qualitative and quantitative analysis, and internal credit ratings; - Acceptable forms of credit support (credit enhancement); - Document retention and file standards; - Credit risk reporting standards including report owner, frequency, and distribution; - Code of ethics and conduct and non-compliance policy; - Policy maintenance and administration requirements; and - Employee acknowledgement and reaffirmation requirements. 	<p>The Credit portion of the RMP describes the credit risk management philosophy, credit risk tolerance, credit limit setting methodology, definitions of the types of credit exposure that are monitored, and definitions of the types of credit enhancements that will be accepted</p> <p>The Procedures Manual goes into additional detail regarding credit risk tolerance, qualification requirements, credit enhancements, assignment of credit limits, monitoring of credit exposures, new counterparty approval, credit limit changes, credit limit extensions, monitoring of exposure, credit risk reporting standards, and credit file maintenance and document retention guidelines.</p> <p>The credit documentation does not discuss potential exposure and some of the descriptions of the credit analysis seem to be out-of-date and not reflective of how the process is currently performed.</p>		<p>See recommendation noted above in section 2.1.</p>	<p>Agreed.</p> <p>SCL will develop an internal work plan for incorporating the recommendations that relate to the Procedures Manual. This work plan will establish responsibility for completion, an expected timeline, and a mechanism for tracking progress towards that goal. Revisions to the Procedure Manual will be subject to final approval by the ROC to become effective.</p>
3.				
<p>3.1 - Credit documentation refers to legal and non-legal documents that provide written reference on how contracting parties will perform during the contract's life.</p>	<p>SCL currently has credit documentation in its counterparty contracts, as well as in credit agreements and credit enhancements</p>		<p>No recommendation at this time, as this appears to be generally in line with our understanding of Prevalent Practices.</p>	

Prevalent Practice	SCL's Current Practice	Categorization	Recommendation	Management Response
3.2 - A business' contract management department, legal and credit groups work together to identify a list of requisite legal documents that serve as forms of credit mitigation in the event of non-performance or default.	SCL currently performs this practice and has documentation related to what types of credit mitigation are acceptable.	✓	No recommendation at this time, as this appears to be generally in line with our understanding of Prevalent Practices.	
3.3 - Original credit documentation is stored in a disaster-proof facility, usually at an off-site location.	Credit documentation (specifically credit enhancement documentation) is filed in normal file cabinets and is not kept in a secure and fireproof area and could be damaged or destroyed in the event of a fire.		SCL should consider maintaining credit enhancement documentation in a more secure environment such as a disaster proof facility such as a safe or an off-site and secure location.	Agreed Implementation of this recommendation is currently underway.
3.4 - Access to the credit files is restricted, with formal check-in/check-out procedures.	There are informal check-in/check-out procedures.		SCL could consider formalizing check-in and check-out procedures for all credit files.	Agreed Implementation of this recommendation is currently underway.
3.5 - Parental guarantees and submitted forms of credit support are always forwarded to the Legal Department for review and approval.	SCL currently performs this practice.	✓	No recommendation at this time, as this appears to be generally in line with our understanding of Prevalent Practices.	
3.6 - Credit support is conditionally accepted upon legal review and approval. Upon acceptance of credit support, leading practices require credit departments to have the capability to track and monitor expiry and "trigger events" (e.g., rating downgrade).	SCL currently performs this practice and monitors counterparty events via a variety of channels.	✓	No recommendation at this time, as this appears to be generally in line with our understanding of Prevalent Practices.	
4.				
4.1 - Counterparty assessment represents the quantitative and qualitative analysis conducted to determine counterparty creditworthiness.	SCL uses a combination of quantitative (external ratings, financial ratios) and qualitative (stable management, adequate credit facilities, market and industry information, etc.) to determine counterparty's creditworthiness.	✓	No recommendation at this time, as this appears to be generally in line with our understanding of Prevalent Practices.	
4.2 - Counterparty assessment methodologies incorporate two key processes in determining creditworthiness – 1) credit scoring and 2) risk rating.	SCL's credit methodology incorporates both credit scoring and risk rating. SCL sets a Cap on the amount of credit allowed to be extended to a counterparty based on its Moody's KMV implied rating. The credit methodology has been revised so that depending on where the counterparty is placed within the credit framework, it starts at 100% of the qualifying credit limit (based on Moody's KMV) then	✓	No recommendation at this time, as this appears to be generally in line with our understanding of Prevalent Practices.	

Prevalent Practice	SCL's Current Practice	Categorization	Recommendation	Management Response
	steps-down, all the way to a \$0 credit limit if necessary, based on both the financial analysis and qualitative information.			
4.3 - Counterparty assessment methodology is based on a framework of financial ratios, relative weightings, external agency ratings, analyst reports and professional industry judgment to determine probability of default.	See comments above in section 4.2.		No recommendation at this time, as this appears to be generally in line with our understanding of Prevalent Practices.	
4.4 - The credit scoring methodology is clearly documented in a credit procedure manual to ensure consistent application regardless of who is performing the assessment.	The Procedures Manual version 06182010 includes a description of a credit scoring model, however the description does not go into complete detail as to how the credit scoring methodology is performed. It is our understanding that the scoring methodology starts with the credit ratings assigned by Moody's KMV and then modifies this score based on quantitative and qualitative reviews performed by the Credit Analyst. See fuller description in Section 4.2 above.		SCL should update the Procedures Manual to include the a more complete and accurate description of the current credit scoring methodology.	Agreed. SCL will develop an internal work plan for incorporating the recommendations that relate to the Procedures Manual. This work plan will establish responsibility for completion, an expected timeline, and a mechanism for tracking progress towards that goal. Revisions to the Procedure Manual will be subject to final approval by the ROC to become effective.
4.5 - Internally developed risk rating systems are regularly validated for reasonableness to ensure they do not significantly deviate from independent external ratings (i.e., S&P, Moody's, and Fitch).	SCL currently develops their internally assigned credit rating and credit limits based on the process described in 4.2 above.		SCL should also consider monitoring the performance of their counterparties against the assigned credit rating.	Agreed. SCL will consider the potential benefits of such enhanced monitoring.
4.6 - The assigned risk ratings are typically measured against actual performance in order to validate the effectiveness of the risk rating methodology.	At a minimum, the Credit function performs an annual review of each counterparty to evaluate creditworthiness. The Credit function also monitors news sources and receives notifications for updated financials of SCL's counterparties, and updates the Scoring Model as appropriate. In addition, SCL maintains a Counterparty Watch List for counterparties within 20% of its credit limit or which represent significant credit risk or exposures (those counterparties with MTM exposure of \$1 million or above or more than 10% of total credit exposure). The Credit function closely monitors these counterparties and issues a weekly report which includes exposure amount, counterparty financial		No recommendation at this time, as this appears to be generally in line with our understanding of Prevalent Practices.	

Prevalent Practice	SCL's Current Practice	Categorization	Recommendation	Management Response
	information, and recent news items.			
5.				
5.1 - Limit setting decisions are guided by a credit limit structure developed by a risk oversight committee and approved by Executive Management.	Credit limits are developed using the credit methodology which was approved by the ROC and are constrained to the Credit Threshold set by the CFO. The ROD develops a proposed credit limit and presents it to the CFO for approval.	✓	No recommendation at this time, as this appears to be generally in line with our understanding of Prevalent Practices.	
5.2 - The credit limit structure is reviewed annually, or more frequently as needed, by the RMC. The RMC should also review and re-approve the risk limits annually, or more frequently, if needed.	The credit limit structure is reviewed annually or as required by changes in market or counterparty conditions.	✓	No recommendation at this time, as this appears to be generally in line with our understanding of Prevalent Practices.	
5.3 - At a minimum, organizations utilize the following credit limit types: <ul style="list-style-type: none"> - A/R limits; - MTM limits; - Maximum Current Exposure Limits (the sum of A/R and MTM limits); and - Some companies have established separate A/R and MTM limits to control each exposure type. Separate A/R limits control slow pay or delinquent payment behavior. MTM limits control the replacement cost of in-the-money contracts held by the company. Typically, counterparty creditworthiness and net worth are the primary drivers in determining a credit limit.	SCL establishes and monitors maximum current exposure limits for each counterparty. This exposure limit is the sum of the Settlement Exposure (AP + current delivered but not billed) and the MTM Exposure.	✓	No recommendation at this time, as this appears to be generally in line with our understanding of Prevalent Practices.	
5.4 - Manage and administer limits through a technology application integrated with or part of the energy transacting and risk management system	SCL manually enters the credit limit information into the Power Ops application. The Credit Window in Power Ops displays remaining available credit ("RAC"), which is the credit limit less the rolling forward 60-day expected accounts receivable balance which is used by transacting personnel to determine if a counterparty is within its credit limit. Our testing of transactions showed that the remaining available credit amounts displayed on the deal ticket in the	☞	SCL should continue to test and monitor the newly implemented trading and risk management system to make sure it appropriately facilitates credit limit management in a more integrated manner in order to reduce the potential for manual errors. SCL should also address the issues associated with the deal tickets containing inaccurate information regarding credit exposure.	Agreed. Robust testing of the new TRM system is currently underway. Agreed. SCL will evaluate the timeframe to full TRM implementation and determine the cost/benefit of correcting this deficiency prior to retirement of the current system.

Prevalent Practice	SCL's Current Practice	Categorization	Recommendation	Management Response
	<p>testing sample were not accurate.</p> <p>This process is changing as the new Trading and Risk Management System becomes operational. Credit limit information is entered into the trading and risk management system which then monitors credit exposures against those limits.</p>			
<p>5.5 - Credit limits can be viewed in a single system by traders, marketers and risk management at any point in time.</p>	<p>Credit issues a daily credit report that details the available credit for the various counterparties. Traders can also view credit limits in the Credit Window of Power Ops.</p> <p>However, the RAC amounts displayed in the Credit Window are not consistent with the RAC amounts reported in the weekly Credit Exposure report. The weekly Credit Exposure report includes forward MTM amounts in its calculation (which Power Ops cannot do). This could potentially result in PMD personnel entering into transactions with counterparties which do not have available credit as a result of a forward MTM position.</p> <p>As noted above, this process is changing as the new Trading and Risk Management System becomes operational. Credit limit information is entered into the trading and risk management system which then monitors credit exposures against those limits.</p>		<p>SCL should continue to test and monitor the newly implemented trading and risk management system to make sure it appropriately facilitates credit limit management in a more integrated manner in order to reduce the potential for manual errors.</p> <p>In the short term, SCL should consider generating a daily Credit Exposure Report that includes MTM Exposure for any counterparty that is within 20% of their credit limit.</p>	<p>Agreed.</p> <p>Robust testing of the new TRM system is currently underway.</p> <p>Agreed.</p> <p>SCL will evaluate the potential benefit of such enhanced reporting.</p>
<p>5.6 - Re-evaluation of counterparty limits occurs either annually, on the anniversary date, or more frequently as market or counterparty financial conditions change.</p>	<p>At a minimum, the Credit function performs an annual review of counterparty limits. The Credit function also monitors news sources and receives notifications for updated financials of SCL's counterparties, and updates the Scoring Model as appropriate.</p>		<p>No recommendation at this time, as this appears to be generally in line with our understanding of Prevalent Practices.</p>	
6.				
<p>6.1 - Total credit exposure represents the total financial loss in the event of counterparty default and is commonly conveyed as the sum of two components – 1) current exposure and 2) potential exposure.</p>	<p>SCL only considers current exposure in monitoring total counterparty exposure. SCL does not include potential future exposure in its credit evaluation or reporting.</p>		<p>SCL should consider including potential exposure in its credit exposure reporting.</p> <p>In order to support this analysis, SCL may consider building out its quantitative capabilities within the risk function.</p>	<p>Agreed.</p> <p>SCL will evaluate the potential benefit of such enhanced reporting.</p> <p>The process is currently underway to fill two vacant positions within the Risk Oversight Division. The skills being sought will greatly</p>

Prevalent Practice	SCL's Current Practice	Categorization	Recommendation	Management Response
				strengthen the ROD in this area.
6.2 - Netting is utilized to mitigate credit risk.	SCL currently performs this practice.	✓	No recommendation at this time, as this appears to be generally in line with our understanding of Prevalent Practices.	
6.3 - If collateral is held, organizations typically apply the net value of collateral held as an offset to current exposure. Collateral offset comes in the form of cash deposits (i.e., prepayment) and letters of credit. Parental guarantees are not typically applied as an offset to exposure.	SCL takes the following credit enhancements as collateral. Prepayments and letters of credit are offset against current exposure.	✓	No recommendation at this time, as this appears to be generally in line with our understanding of Prevalent Practices.	
6.4 - Organizations calculate total credit exposure on a <i>daily</i> basis by counterparty only.	Total credit exposure is calculated on a weekly basis. RAC is calculated in the Credit Window of Power Ops on a real time basis; however this only includes the settlement exposure value. As the new system is implemented, credit will be updated on a real-time basis. However, formal credit exposure calculations with reporting to management are only expected to be conducted on a weekly basis.	👉	As the new system is implemented, SCL could consider calculating total credit exposure on a daily basis. Given SCL's position in the market as a net seller, it is critical that it actively monitors and manages its credit exposure position. In the short term, SCL should consider generating a daily Credit Exposure Report that includes MTM Exposure for any counterparty that is within 20% of their credit limit.	Agreed. SCL will evaluate the potential benefit of such enhanced reporting.
6.5 - Organizations with multiple business lines that transact with the same counterparty have developed the capability to aggregate exposures across business lines and manage them across one global limit at the enterprise level.	Not applicable	✓	Not applicable	
6.6 - Organizations aggregate credit exposures across risk factors such as rating class, customer class, industry, geography, or other exogenous variables.	SCL aggregates credit exposures by counterparty class (credit rating) as part of the ROC Weekly Status Reports. All of SCL's business is located in one geographic area so there is no need to aggregate exposures by this variable. Additionally, it appears that SCL primarily sells power to utilities and major financial institutions.	👉	In addition to aggregating credit exposures by counterparty class, SCL should consider aggregating credit exposures by industry.	Disagree. Given the limited nature of transactions SCL engages in, it does not have sufficient exposure to particular industries to warrant such monitoring.
7.				
7.1 - Organizations have established clear guidelines and controls to monitor the quality of credit support in the same rigorous manner as the underlying counterparty, especially bank-issued	SCL describes the use and management of credit enhancements in its RMP.	✓	No recommendation at this time, as this appears to be generally in line with our understanding of Prevalent Practices.	

Prevalent Practice	SCL's Current Practice	Categorization	Recommendation	Management Response
letters of credit and parental guarantees.				
<p>7.2 - Credit function closely tracks salient collateral details for administrative purposes. The most common details tracked include:</p> <ul style="list-style-type: none"> - Name of guarantor or reference entity; - Face value of the enhancement agreement; - Date of expiration; - Renewal requirements; - Trigger events; and - Any limitations (such as being commodity-specific) 	Credit function continually tracks these collateral details by counterparty for administrative purposes.	✓	No recommendation at this time, as this appears to be generally in line with our understanding of Prevalent Practices.	
8.				
8.1 - Credit limit monitoring is a key control to ensure credit exposures are consistent with senior management's credit risk tolerances.	SCL actively monitors credit limits for compliance to its RMP.	✓	No recommendation at this time, as this appears to be generally in line with our understanding of Prevalent Practices.	
8.2 - Limit monitoring is the responsibility of independent credit control staff and is performed and reported daily.	The Risk Oversight Division is responsible to monitor credit exposures versus limits. This is done on a weekly basis.	👉	SCL should consider more frequent monitoring of credit exposures against limits by the ROD. The ROD produces a weekly credit exposure report for the ROC which serves as the primary credit monitoring report for the Credit function. Given SCL's position as a net seller of energy in the market, the Credit function should review the current exposure on a daily basis.	<p>Agreed.</p> <p>SCL will evaluate the potential benefit of such enhanced reporting.</p>
8.3 - Organizations have established warning thresholds to trigger pre-emptive courses of action before a limit is breached. This is typically accomplished by imposing "yellow" and "red" zone limits that act as triggers to develop credit mitigation strategies prior to a full limit excess.	The Credit function has established soft caps to identify counterparties nearing their credit limits. Counterparties within this limit are included in the weekly Counterparty Watch List report.	✓	No recommendation at this time, as this appears to be generally in line with our understanding of Prevalent Practices.	
8.4 - Organizations have developed a formal limit exception process, which defines the necessary approvals and actions to take when a limit or threshold has been violated. Any potential transaction that may cause a limit or threshold excursion is brought to the attention of senior management independent of the trading area for written approval.	<p>The Procedures Manual documents the process in the case that a limit has been violated.</p> <p>In addition, SCL requires a Pre-Deal Risk Assessment Sheet prior to any transaction with a term of seven days or greater. This Pre-Deal Risk Assessment Sheet requires a sign off by the ROD signifying that the targeted counterparties have been reviewed and there is sufficient credit available for the transaction.</p>	✓	No recommendation at this time, as this appears to be generally in line with our understanding of Prevalent Practices.	

Prevalent Practice	SCL's Current Practice	Categorization	Recommendation	Management Response
	Going forward, the process for the Pre-Deal Risk Assessment will be performed within the trading and risk management system, but the concept is the same.			
8.5 - In the event of a credit limit violation, an oversight committee (i.e., RMC) is promptly notified. The Credit, Risk and Transacting Supervisors collectively develop a corrective action plan and recommend it to the RMC for approval.	See comments above in section 8.4.	✓	No recommendation at this time, as this appears to be generally in line with our understanding of Prevalent Practices.	
8.6 - Exposure vs. limit reports and their distribution throughout the organization are clearly defined by risk management policy.	Exposure vs. limit information is contained in the Risk Oversight Council Weekly Status Report. This report and its distribution are defined in the RMP.	✓	No recommendation at this time, as this appears to be generally in line with our understanding of Prevalent Practices.	
9.				
9.1 - Back Office notification of slow pay patterns, delinquency and collection payments to the Credit Department is automated and timely.	The Credit function receives a weekly A/R Aging report. Notification is done manually and is not automated.	✓	No recommendation at this time, as this appears to be generally in line with our understanding of Prevalent Practices.	
9.2 - Credit decisions such as account suspension or limit reduction require timely and accurate collection status and balances.	Credit and A/R personnel work together to identify counterparty accounts that require credit changes or updated collection status.	✓	No recommendation at this time, as this appears to be generally in line with our understanding of Prevalent Practices.	
9.3 - Credit systems typically interface with the accounts receivable system so that exposure amounts are updated with (un)collected amounts on an automated basis.	The interface between A/R and Credit is done manually and on a timely basis.	👉	SCL may consider investing in further application development to automate credit functionality and use of accounts receivable data.	Agreed. SCL will evaluate the potential cost/benefit of such integration.