



Department of Energy

Bonneville Power Administration
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JUN 02 2004

EXECUTIVE OFFICE

In reply refer to: R-3

Mr. Pat Reiten, CEO
Pacific Northwest Generating Cooperative
711 NE Halsey Street
Portland, OR 97232-1268

Dear Mr. Reiten:

Thank you for your letter of April 8, 2004. We appreciate your support for moving forward to develop a workable Beginning State that addresses regional issues as defined by regional stakeholders through the Regional Representatives Group (RRG).

We agree with you that the Regional Proposal, properly structured, has potential to provide significant regional benefits. "One stop shopping" through a single OASIS and adopting common business practices across the Grid West footprint will facilitate economic transactions that do not occur today, reduce the difficulty in scheduling across multiple control areas, and facilitate requests for new service.

Consolidating control areas will improve reliability and generate tens of millions of dollars in savings every year in reduced regulation and other reserves. Using a common flow-based methodology to calculate ATC and TTC across the Grid West footprint will lead to more efficient use of the grid.

Developing consistent procedures and methods adopted by all transmission owners will allow for better coordination and scheduling of planned outages. Increasing efficiency by working together to manage ATC, outage schedules and curtailment practices is an important mechanism we have to keep rate increases manageable as the Northwest economy continues to grow and as new transmission infrastructure is added.

Your letter expresses concern that the Bonneville Power Administration's (BPA) modification of its scheduling practices may make a systematic solution to congestion management more difficult. While we are optimistic that in the Beginning State a comprehensive regional solution will be developed that will provide regional benefits, BPA cannot wait for a regional framework to be established. With the transmission system constraints that now exist, we have no choice but to move forward with interim actions that provide for granting and managing transmission use based on capacity on the constrained paths. As BPA develops an interim fix, we will seek customer input so as to minimize any potential impact. Zonal type scheduling, if adopted by

BPA, will not pre-determine how scheduling will be done by Grid West. It should be noted, however, that certain features of the proposal suggest that some form of Zonal type scheduling may be required. BPA will work through the RRG processes to develop the Beginning State to make sure that BPA's interim practices and procedures do not become an impediment to improved, system-wide scheduling practices.

With respect to your comments relating to regional planning, BPA is encouraged by the Regional Proposal because it embraces "one utility," system-wide planning, including back-stop authority to assure the best projects get built and those transmission owners who benefit contribute to the cost. While BPA prefers the stronger backstop authority of Stage 2 because it contains the ability to respond to chronic commercial congestion, the Regional Proposal is a significant improvement on today's approach. Backstop authority is important because BPA cannot afford to build all of the region's transmission facilities and it is unfair for BPA's customers to bear all the costs of projects, especially when other transmission owners benefit.

As you point out in your letter, there are four separate and distinct decision points before a decision is made to implement the Beginning State. BPA's support for the Regional Proposal is not a decision by BPA to endorse either the Beginning State, which needs further definition, or the Advanced State. BPA has not made a decision on either. Instead, BPA intends to support further development of the Regional Proposal to shape it into a workable, sustainable approach to regional transmission issues—based on regional issues developed by regional interests. BPA will test each stage of development before BPA will support it. This includes the Beginning State.

The key concept is "evolution, not revolution." A phased-in approach allows time to test each stage before evolving further. If a phase is reached where further development is not worth the effort, we agree there should be no reason to move to that stage, including the Advanced State. Implementation of the Beginning State can and must be separated from a decision to implement the Advanced State.

When the proposal has been refined, BPA will then step back to determine whether the Regional Proposal is likely to deliver on its promises. Do the rewards outweigh the risks? Have we minimized costs and reduced risk while providing Grid West the resources it needs to succeed? Are major cost shifts avoided? Is the proposal workable for the Northwest? Is the proposal sustainable over time? Does the Transmission Operating Agreement (TOA) contain adequate provisions requiring the Independent Entity (IE) to honor existing contracts and other BPA obligations? Are the checks and balances in the governance documents and accompanying agreements adequate to ensure the entity is independent of market participants, but responsive to regional needs? Are GTA customers assured quality service at reasonable cost? Does the market monitor have the tools necessary to effectively monitor for abuse? Does the TOA and accompanying markets designs contain adequate off ramps that provide BPA with a practical exit strategy should the IE not deliver on its promise?

Once these and related questions are answered satisfactorily, BPA will make a final determination whether to sign a TOA, the “go-no-go” decision that allows implementation of the Beginning State. Until then, BPA will not have made a final determination to move forward.

An argument often made is that BPA’s support for forming an IE creates a “slippery slope” that inevitably leads to the Advanced State. This is not the case. BPA’s support for the Regional Proposal does not mean that BPA supports implementation of the Advanced State. The proposal calls for the implementation of the Advanced State only if it is determined at a later date that doing so is beneficial to the region. The Advanced State is recognized in the platform because the RRG members realized the entity would need the ability to evolve over time. But there is no agreement among RRG members about the desirability of implementing the various elements of the Advanced State at this time.

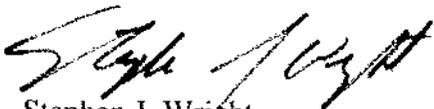
Another reason for recognizing the Advanced State in the Proposal was to build in regional checks and requirements in the governance structure to protect against the possibility that the entity would change despite regional concerns. This reasoning is reflected in the full Proposal on pages 18 and 19 in reference to moving to a financial rights methodology, which your letter notes is an area of serious concern to PNGC.

A sub-group of the RRG is currently developing bylaws to ensure that safeguards are workable, that the entity will consider the best interests of the region in proposing changes, and that the entity demonstrates to regional stakeholders that major changes are beneficial. The TOA needs to include provisions that require the entity to honor BPA’s existing contracts and other BPA obligations, including ratemaking, treaty, environmental and other statutory requirements. In designing the entity’s systems, BPA will retain control over its generation and transmission assets, even though the management and the transmission assets will be done by Grid West. This control, coupled with appropriate termination provisions in the TOA, will give BPA the practical ability to exit the entity should that become necessary to avoid adverse impacts to BPA’s customers.

BPA believes the Regional Proposal has potential but the details of the proposal still need to be worked out before it takes a final form as a workable approach for the region.

We look forward to working with the PNGC and other members of the public power community in further defining a Beginning State that works for the region.

Sincerely,



Stephen J. Wright
Administrator and Chief Executive Officer