Department of Energy

Bonneville Power Administration
P.O. Box 3621
Portland, Oregon 97208-3621

EXECUTIVE OFFICE

SEP 2 3 2014

Mr. Mark E. Reddemann, Chief Executive Officer
Energy Northwest
P.O. Box 968
Richland, WA 99352-0968

Dear Mark:

The Bonneville Power Administration (BPA) and Energy Northwest have been close public power partners for many years. The most obvious example of this partnership is Energy Northwest's Columbia Generating Station (Columbia), which provides a valuable and essential component of BPA's and the region's long-term electric power supply. Columbia is not the only productive endeavor between BPA and Energy Northwest. Behind the scenes, BPA and Energy Northwest have been working closely together to provide enormous financial value to the region for more than 25 years through coordinated management of the debt issued by Energy Northwest for Columbia and Projects 1 and 3; Energy Northwest's other two net-billed projects. These mutually-supported debt management actions have reduced pressure on BPA's revenue requirements and rates innumerable times.

The close association between our two organizations in matters of debt management has also provided extensive relief for the constrained capital funding that BPA and the region face given BPA's limited United States Treasury borrowing authority. Through Energy Northwest and BPA's Debt Optimization Program, Energy Northwest enabled BPA to replenish its revolving United States Treasury borrowing authority by more than $2 billion, which in turn has led and will continue to lead to the funding of essential Federal System capital investments while avoiding difficult regional choices between revenue financing and sub-optimum investment in the Federal System.

Most recently, our financing staffs have brought forward another proposal, regional cooperation debt refinancing. As with the Debt Optimization initiative, the regional cooperation debt refinancing is based on coordinated financial management to bring value to the region. In short, this opportunity involves the extension of the average maturity of Energy Northwest's net-billed debt and the early repayment or retirement of BPA's United States Treasury obligations. The proposal promises to reshape and lower the cost of BPA's overall debt portfolio in ways that could save over a billion dollars for regional ratepayers. For BPA, the proposal offers the potential to keep BPA's rates attractive to regional ratepayers for years to come, well beyond the end of the Regional Dialogue Power Sales Agreements in 2028. It also brings the potential to reduce BPA's access to capital shortfall, which we and the region have faced since at least the early 1990's. The repayment of federal obligations, which the proposal will assist in enabling, is at the core of BPA's statutory responsibility both in the establishment of its rates and in the conduct of its business. The proposal is also consistent with sound business principles. A reduced long-term aggregate debt service profile will assist BPA in maintaining its position as a low-cost power supply choice for the region.

In great part because of your leadership and collaborative approach, our shared stakeholder base in the region is reaching a core level of awareness and support for the proposal. Getting to this point has not been easy. Understanding the potential value of the proposal involves building a working understanding of the complex and sometimes counterintuitive inter-relationships among BPA's overall debt service obligations, Energy Northwest's net-billed project debt service obligations and BPA's rates. It also involves an acceptance of managing all debt obligations borne by ratepayers through BPA's rates on an integrated, optimized basis. Both the daunting amounts at issue and earnestly held expectations about the wisdom of paying off Projects 1 and 3 debt as previously scheduled have made the outreach and education process even more challenging. Your efforts in this process have been exemplary.

I now believe that most regional parties understand and appreciate the underlying soundness of the proposal. Furthermore, no parties have raised substantial concerns that we have not ourselves identified and fully addressed. We now have the level of regional support needed to proceed with the next phase of executing the regional cooperation debt refinancing.

To help move things forward, you asked us to describe the key elements associated with implementing the proposal. The attached term sheet outlines our proposed process for proceeding with this important opportunity.

Our joint efforts coupled with sound, flexible financial management will both ensure our combined economic value for the region and continue to provide for adequate operations and maintenance and capital investment funding at Columbia to support continued safe, reliable and cost-effective operation.

It is our expectation that our shared spirit of collaborative action in the best interests of the region will continue to advance the regional cooperation debt refinancing as we move into implementation. We look forward to successful execution of the opportunity and I thank you and your staff for all of the insight and hard work that Energy Northwest has provided in bringing us to this point.

Sincerely,

Elliot E. Mainzer
Administrator and Chief Executive Officer

Enclosure:
Regional Cooperation Debt Term Sheet

Regional Cooperation Debt – Term Sheet

Regional Cooperation Debt Program

- The Regional Cooperation Debt Refinancing Program (Program) is the extension of the average maturity of BPA-supported Energy Northwest net-billed project bonds (Columbia Generating Station, Project 1 and Project 3) on an integrated basis with BPA's overall debt portfolio, as described herein.
- To reflect the notion that Energy Northwest debt extended under the Regional Cooperation Debt Refinancing Program is debt borne by the Region in BPA's rates and is being extended for the benefit of the region's ratepayers as an integral part of all of BPA's debt, all such Columbia Generating Station, Project 1 and Project 3 debt so extended will be reflected where practical and germane as "Regional Cooperation Debt." While all of the net billed bonds can be viewed as regionally-supported debt, it is particularly important for the region to appreciate that Energy Northwest is taking action in furtherance of the Program with a broad view of its Regional responsibilities and is willing for the good of the region to carry the Regional Cooperation Debt on its books as a liability for a longer period than previously scheduled.
- Each of the Program's bond financing transactions must be approved by the Energy Northwest Executive Board.
- BPA will provide to Energy Northwest information on BPA's financial operations with respect to the Program. BPA will provide to Energy Northwest the information detailed in the Financial Information Annual Update section annually to help it assess the continuing progress of the Program. Energy Northwest may determine that more or less information may be needed at a given point in time and BPA and Energy Northwest will work to assure that the appropriate level of transparency is provided as the Program is implemented.

Regional Cooperation Debt for Columbia Generating Station

- While it is preferred that revenues freed up from Columbia debt extension be used to repay within a reasonable period of time an amount of Federal debt equal to the Columbia debt extended, each transaction should allow for the flexibility to be structured in a manner that provides the most overall benefit to the region, as determined through a public process involving BPA customers.

Regional Cooperation Debt for Projects 1 and 3

- Annually, BPA will demonstrate that the prepayment of federal appropriations repayment obligations has been made (or within a reasonable period will be made) in an amount equal to the related Projects 1 and 3 Regional Cooperation Debt.
- The issuance of Projects 1 and 3 Regional Cooperation Debt is expected to occur annually through Energy Northwest's Fiscal Year 2018. BPA will demonstrate that, as of the end of its Fiscal Year 2018, the Program resulted in reducing the aggregate weighted average maturity of the combination of (i) Projects 1 and 3 debt, and (ii) federal appropriations repayment obligations. The demonstration will compare the reduction in the aggregate weighted average maturity of federal appropriations repayment obligations that were prepaid as a result of Projects 1and 3 Regional Cooperation Debt issuances to the amount by which the aggregate weighted average maturity of the Projects 1 and 3 debt was increased under the Program.
- BPA's actions under the Program must be consistent with applicable law, including BPA's statutory obligation to pay federal obligations after meeting non-federal obligations.

Financial Information Annual Update Section

Capital Review

- Capital Investment Review Update
- Historical Capital Spending (10 yr. history)
- Proposed Capital Spending (10 yr. CIR projection)

Access to Capital

- Sources of Capital Background
- Treasury Borrowing Authority Update

BPA Operation and Financial Metrics

- Order in Which BPA's Costs are Met
- Historical Power Rates
- BPA Rates Assure Cost Recovery
- Operating Revenues & Expenses
- Financial Reserves
- Days Liquidity on Hand
- Financial Performance and Coverage
    - Non-Federal Debt Service Coverage Ratio
    - Total Debt Service Coverage Ratio
- Debt Ratio
- Bond Ratings (S&P, Moody's, Fitch)

Debt Management

- Total Debt Liabilities over Time
- History of Annual Debt Payments
- Total Debt Pie Chart
- BPA Current Debt Service
    - Power
    - Transmission
- Upcoming Debt Transactions
- Report on Use of Freed Up Cash from EN Debt Refinancing
    - E.g. showing that highest interest rate Federal Debt was paid off