



Department of Energy

Bonneville Power Administration
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EXECUTIVE OFFICE

January 22, 2004

In reply refer to: P-6

NOTE: This close-out letter was mailed to all regional public utilities, public utility organizations, IOUs, the four state commissions.

Midnight Wednesday, January 21, was the last opportunity for signing on to a proposed settlement of lawsuits brought by public utility customers regarding the level of benefits going to investor-owned utility customers. As most of you know, the settlement needed approval by all litigants to pass, which it did not get. However, BPA received formal expressions of support from 86 public utilities, which included some non-litigants, while six expressed opposition. We at BPA are disappointed that the settlement was not successful because we believed it was the best avenue for near-term rate relief. Still, I want to thank the many utility managers and staff who invested many hours over a period of months to develop and review the proposal. The support it received is a great testament to the hard work that went into it.

The obvious question is "what's next?" The settlement's failure will not deter us from working to bring rates down. Regardless of the outcome of the settlement, we will continue to vigorously pursue the \$100 million in cost cuts/revenue enhancements that was part of the settlement conditions. We also are willing to pursue alternate means of capturing some or all of the benefits of the settlement, but only if they meet the principles provided below, which were outlined in our earlier letter:

- An alternative needs broad support of those affected by it;
- An alternative must provide immediate rate reduction for public power customers;
- An alternative must not rely on abrogating contracts, ignoring environmental commitments, jeopardizing reliability or increasing risk to U.S. Treasury payments.

However, starting now, we must start paying greater attention to the future. There are major issues on the horizon, including post-2006 power rates, post-2005 transmission rates, a cost-effective fish and wildlife program and infrastructure investments—to name just some of the issues ahead. Not the least of these is the fact that BPA has over 3,000 average megawatts of load uncertainty for the post-2006 period. We have been deferring work on these issues for too long and now need to address them.

We look forward to working with you on these important issues in a number of venues, most notably the Regional Dialogue and Transmission's Programs in Review. We also will continue our efforts that were embedded in the settlement documents to increase transparency regarding

BPA's financials by working with the Customer Collaborative and the Power Net Revenue Sounding Board.

I expect some of our customers to press for revisiting the Safety Net Cost Recovery Adjustment Clause (CRAC) decisions we made last year. A major reality we face is that rates follow costs along with secondary sales revenues. The settlement would have resulted in \$470 million in cost reductions and deferrals for the remainder of this rate period. Of that, \$200 million represents costs that would otherwise be recovered from the Load-based CRAC, and \$270 million represents deferrals that would otherwise be recovered through the Safety Net CRAC. We will continue our strenuous efforts to cut costs and enhance revenues, but nothing of this same magnitude is on the horizon.

Another reality is that BPA's financial outlook has not fundamentally changed since we adopted power rates in September. The forecast for water conditions for '04 is slightly below normal. While wholesale market prices seem high, thus far they are no higher than those forecast for this year when BPA adopted its power rates.

Overall, our '04 average power rates will be about 1 percent below our '03 rates. At this point all decisions for these rates have been made, and with the demise of the settlement there are no decision points left with respect to '04 rates. Our main opportunity now is to continue our progress on cost reduction and revenue enhancement to minimize the size of the Safety Net CRAC this October. We also will continue to hope that this year does not end up being the fourth straight year of below average water conditions.

I look forward to your input on the many issues ahead of us. I want again to thank those who worked so hard on the settlement. Despite its failure, I continue to believe our best chances for success lie in a future where we all work closely together.

Sincerely,

/s/ Stephen J. Wright

Stephen J. Wright
Administrator and Chief Executive Officer