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Steve Wright, Administrator  
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PO Box 3621  
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Submitted electronically at: [comments@bpa.gov](mailto:comments@bpa.gov)

Dear Mr. Wright,

Thank you for taking additional public comments regarding the 2010 Integrated Program Review (IPR) process. We appreciate that in the BPA draft Close Out letter for IPR the overall size of a potential wholesale power rate increase related to expenses was reduced from 14% to 7%, and that BPA responded favorably to many of Northwest Requirements Utilities' recommendations previously submitted. In this set of recommendations we have developed a package of proposed reductions and shifts between expense and debt funding that have the consequence of reducing the 7% number to 4.2%. While these recommendations in all cases may not reflect the views of all of our members, we believe they will be strongly supported as a package that will reduce upward pressure on local retail rates, and will continue to promote BPA's operation under sound business principles. Each item is described in the text, and a financial summary of our recommendations is provided at the end of the document.

This is an important process as it will set a major part of the revenue requirements for the FY 2012- 2013 rate period. This will also be the first rate period under the Tiered Rates Methodology which will add its own challenges and rate level uncertainty.

NRU staff has been actively engaged in the IPR process and many managers of NRU member utilities attended the managers' meetings regarding this topic. On average the cost of BPA power and transmission purchases make up about 60 percent of these utilities' cost of service. As you heard in the meetings, NRU's members are concerned about a combination of compounding factors that will materially impact their wholesale power costs from BPA beginning October 1, 2011. These include:

- After incorporating the revisions pursuant to the draft IPR recommendations a potential forecast rate increase due solely to increasing costs in the 7% range.
- Significant further rate increase pressure due to the cost of risk mitigation tied to maintaining adequate financial reserves.
- Concerns related to the uncertainty about the value of the costs and revenue credits that are unknown at this time and have not even been included in the data we are now seeing. These include residential exchange benefits, costs of DSI service and the dollar value of secondary sales.
- A likely inherent increase in wholesale power rates and uncertainty for many members associated with the implementation of the Tiered Rates Methodology.
- An obligation to purchase power at a Tier 2 rate or non-federal power supply to cover above High Water Mark loads, where such power may be twice or more as expensive as BPA power at Tier 1 rate.

BPA did take a number of actions as a result of comments received by NRU and other parties, and these are incorporated in the draft response issued on July 9, 2010. Of the total power related increase of \$261 million from average FY 2010 to 2011 to average FY 2012 to 2013, BPA has proposed cost reductions of \$123 million and program suspensions of \$3 million. About 95 percent of these cost reductions came from just three areas; reduced CGS debt service and fuel costs and the removal of the cost of a proposed insurance policy. Reductions to BPA's Agency Services costs and Power non-generating operations costs totaled \$5 million.

Further reductions are required, and we appreciate you and your staff's receptivity to receiving additional input from customer representatives. As we heard very clearly in the BPA July 13th Manager's meeting from BPA's customers, that while BPA's costs are increasing, the Agency should target a single digit rate increase and find ways to reduce its costs and manage its debt so as to be able to live within a rate increase of this magnitude. Such an objective needs to be accomplished in the context of "sound business principles." Therefore, in the interim, the NRU staff has worked to identify further reductions in cost that we believe are prudent, to improve the potential for a single digit rate increase.

In addition to the increasing costs of wholesale power supply, our members are faced with cost increases in running distribution systems, often for new and expanding functional responsibilities. WECC compliance, RPS requirements, and increasing operating expenses, which when combined with rising wholesale power costs is very challenging. We anticipate that the potential size of the rate increase may be substantially mitigated by favorable treatment on such issues as debt structure, nuclear fuel costs, and the treatment of conservation costs. Even if these issues are successfully addressed the rate increase will still be significant and will require diligent attention to the budgets of

other Federal Agencies such as the Corps and Bureau and Energy Northwest, but also the internal costs of BPA.

As a backdrop for our comments we would like to highlight the poor economic condition in the service territories of our member utilities. Below are the average unemployment rates for May 2010 for the counties served by the largest members of NRU. A significant BPA rate increase will only add to the economic ills that are being experienced at these utilities.

Central Lincoln PUD	12%
Flathead Electric	12%
Inland Power & Light	8%
Oregon Trail Electric	13%
Richland	7%
Lower Valley Energy	7%
Peninsula Light	9%
McMinnville Water & Light	11%
Columbia River PUD	11%
Wells Rural Electric	8%
Salem Electric	10%
Tillamook County PUD	10%

### **The IPR Process**

Before we begin our specific comments we would like to make some observations about the IPR process itself. BPA and other entity staff provided a wealth of material in support of the need for increased funding in many areas. At times the sheer amount of material seemed a bit daunting. We appreciate their efforts. However, our concern is that while the need for increased funding was described in detail, we did not get the impression that the programs were evaluated “from the ground up” by BPA and the other entities, in the context of using current rates as a starting point. We believe that there are functions of a lower priority that continue to be performed but could be eliminated or reduced in order to provide funding for programs that are of a higher priority. It is very difficult for those looking in from the outside to know what costs are critical and what are of a lower priority. This is really known only by those people that operate these programs.

We look forward to working with BPA staff as they develop IPR for the future, particularly from the perspective of how proposed spending levels are evaluated in the context of current rates.

## **Non-Federal Debt Service**

BPA and the customers have spent time during this process looking at the structure of Energy Northwest (ENW) debt for WNP-1, -3 and the Columbia Generating Station (CGS). Currently this debt is to be nearly paid off in 2019. Between 2012 and 2018 amortization of Federal debt falls off steeply (it is actually forecast to go to zero in 2015 through 2017). Over the same period amortization of non-federal debt (primarily Energy Northwest debt) grows to \$722 million in 2017 and then drops to \$68 million in 2019. The authors of this debt structure were concerned that these debts not be imposed on future rate payers. However, CGS is licensed to 2024 and the customers are expected to benefit from the output of the plant until at least 2024.

Under debt service restructuring Scenario B developed by BPA staff, total BPA debt service costs are lower by \$108 million per year on average through 2017 (this covers the next three rate periods). Costs are then higher in 2019 and 2020 by \$155 million per year. After 2020, costs are higher by about \$50 million per year through the end of the new power sales contract. The net present value of the savings under this approach is \$196 million at 8% (\$172 million NPV at 6%). The 2012 component of these transactions cannot be completed prior to the final BPA rate proposal unless the transaction is “hedged”. The total amount of debt service over 20 years under scenario B is slightly higher than the base case. This scenario requires actions in both 2011 and 2012 (which is the first year of the next rate period) and produces the largest savings. The scenario would extend \$775 million in CGS principal and repay \$274 million in callable Project 1 and 3 debt in 2011 and 2012 (earlier than under the current payment schedule).

NRU staff recommends that BPA and ENW pursue Scenario B. Scenario B provides the highest level of rate relief and also has a lower net present value when compared to the current debt service stream. We should now take steps to address the issues of how the 2012 portion of this would be accomplished. In this effort we ask that ENW, BPA and the customers work together in this analysis to ensure that we are achieving the most efficient overall debt service profile for ENW, other non-federal debt, and federal bonds and appropriations. We do not advocate moving the WNP-1 or -3 debt service beyond 2018. While this is an important issue that needs broad public discussion, we note that the NRU staff is supporting recommendations already included in BPA’s draft Close Out letter, and therefore there is no further cost reduction specified in this area.

## **Columbia Generation Station Fuel Costs**

When 2010/2011 CGS costs are compared to 2012/2013 costs, we see an increase that is almost totally made up of two factors: the increase in fuel costs and the reduction in fuel revenues. When these two are added together, 97% of the \$55 million average annual cost increase is explained. This increase is due to the ending of the relatively low-cost fuel purchases under the DOE pilot program,

and its replacement with market fuel purchases. One way that the rate impact of these high fuel costs can be ameliorated is to spread their recovery over the fuel burn. Utilities around the nation that we have contacted amortize nuclear fuel purchases over the fuel burn, rather than expense them in the year the fuel is purchased.

In further discussions with BPA staff on this topic given the workings of the repayment study we have found that there may be various ways to reflect the payment of fuel costs over time that could increase current power rates or decrease them. We suggest that BPA, the customers and ENW continue to work together to reduce fuel costs for the FY 2012 – FY 2013 rate period by shaping these costs over the ratepayers that will benefit from this fuel. We continue to believe that by amortizing fuel costs over the burn money can be saved in the next rate period. We estimate that these savings could add an additional \$20 million per year. We strongly encourage BPA and ENW and the customers to further these discussions in time to get any reductions into the revenue requirement for FY 2012 and 2013. Further technical discussions relating to the fuel purchase and accounting treatment will continue beyond the July 29<sup>th</sup> IPR written comment deadline. Based on the outcome of those discussions, NRU reserves the right to modify this recommendation, to either increase or decrease the assumed amount of saving as the case may be, based on the best information available.

### **Corps and Bureau Non-routine Extraordinary Maintenance Costs**

A rather disconcerting finding during this process has been the sheer amount of non-routine extraordinary maintenance (NREX) at the Corps and Bureau projects that needs to be addressed. About 15% of O&M program costs are for NREX, the large infrequent activities associated with returning failed units to service, repairing gates and other large equipment and structures, as well as the work required for overhauling the big 805 and 600 MW units in the Grand Coulee Third Power Plant. This translates into an average increase in costs of \$47 million per year in expenses for the rate period. These costs are being treated as an expense even though this represents maintenance and repairs on long-lived assets. This is really only the start. These costs will be at a very high level for years as the Grand Coulee Third Powerhouse is refurbished. BPA needs to do everything it can to identify those assets that can be capitalized and paid for over the life of these facilities. The NREX requirements for this project alone are \$16.6 M in FY 2012 and \$20.7 M in FY 2013 and continue at or above this level through FY 2023.

In the presentation materials related to the issue of NREX, BPA found that in their review of the accounting practices of other entities that additions and betterments are capitalized. The Western Area Power Administration uses the following definition of Betterment.

“Betterments are defined as a substantial enlargement or improvement of existing structures, facilities, or equipment by replacement or improvement of parts without replacement of a

complete unit of property, which has the effect of extending the useful life of the property, increasing its capacity, lowering its operating cost, or otherwise adding to its worth through the benefit it can yield”.

We suggest that such a definition should be useful as BPA, the Corps and Bureau examine individual investments in their consideration of those assets that should be capitalized. In our view another way to approach this issue would be to seek a special dispensation for the accounting treatment of the Grand Coulee Third Power Plant given its size, the extended time that it will take to perform this overhaul and critical importance to the system of these units. Please note we are not recommending that the entire NREX program be capitalized, but only a portion of the Grand Coulee Third Powerhouse Overhaul. Therefore expenses for this overhaul are reduced by an estimated \$10 M per year.

**Corps and Reclamation O&M Expense Programs**

NRU recognizes the need for a significant investment in O&M to maintain the structural integrity of the FCRPS and to perform maintenance activities that in the long run hold down the costs of future repairs and renovations if components of the system are deteriorating. While this is the case, the needs of the FCRPS have to be balanced against the needs of distribution utilities to maintain their own systems, and the extent to which a significant BPA rate increase effectively precludes utilities from raising rates to cover their own internal costs for needed repairs.

In reviewing the IPR Bureau of Reclamation and Corps of Engineers 5% Reduction Scenario, and then delineating the distinction between “high” and “medium” reduction project descriptions, the following table can be constructed.

Agency	IPR total	All Reductions	Medium Priority	Med % of Total
Reclamation 12	113,672	5,684	1,620	1.43%
Reclamation 13	121,591	6,080	1,855	1.53%
Corps 2012	214,000	10,700	600	0.28%
Corps 2013	221,000	11,050	1,845	0.83%
2 Year Total	670,267	16,384	5,920	0.88%

It is also noteworthy that the Corps and Reclamation caveat the reductions with a statement that the activities are two years out and “*the priority to fund or not fund an item may change based on agency or system priorities at that time.*”

NRU recommends that BPA negotiate with the Corps and Bureau for at least a 1.5% across the board reduction expenses that would be achieved by project/activity elimination or deferral. Using a 2-year

average of \$335 M in O&M expenses, this would translate into a \$5.0 M reduction per year in BPA supported O&M for these agencies. We have no targeted programs for these reductions and would leave that to the discretion of the agencies. We understand that this level of reductions exceeds what the Corps and Bureau identified in their “medium” impact descriptions of reductions. However, this is still a very modest reduction in light of the fact that the O&M program expense proposed in IPR increases over 2011 IPR levels 13.1% for FY 2012 and 18.1% for FY 2013.

### **FCRPS Cultural Resources Program**

The FCRPS Cultural Resources Program, which has been funded at about \$4.5 M per year through FY 2011 is proposed to increase to about \$8.6 M on average for FY 2012 – FY 2013. This is over a 90% increase, and is above and beyond the substantial new financial obligations BPA has associated with the Fish Accords and MOAs relating to the Bi-Op. Given current economic conditions NRU does not support an increase of this magnitude, even if a portion of the increase is attributable to a transfer of some Reclamation costs previously in other O&M categories. NRU recommends that the \$8.6 M budget be reduced by \$2.0 M to \$6.6 M. This would still allow for a nearly 50% increase in the overall budget.

### **Fish and Wildlife Costs**

The May 10, 2010 IPR “Overview Workshop” shows the costs of the Fish and Wildlife Programs. Actual costs for 2009 were about \$179 M. Now for 2012 and 2013 they go to \$250 M and \$254 M, an increase of over 40%. These cost increases are largely due to the implementation of the Fish Accords with the tribes and state agencies. NRU members did not oppose the Fish Accords, and did not oppose the FCRPS Bi-Op. We are willing to pay a reasonable price for fish and wildlife programs. However, all of this spending occurs in the context of BPA’s rapidly declining reserves for Power Services. To help alleviate this problem BPA, the agencies and tribes need to take a hard look at the ramp rate for these programs to see if the funding being requested can be spent in a cost effective manner. If not, then these costs should be removed from the funding requests for FY 2012 and 2013. We understand that contracts for the MOA projects have the automatic 2.5% increase in funding levels each year. This automatic funding level increase occurs whether or not the funding is actually needed. BPA should work with the agencies and tribes to see if this funding level is needed for each year. If not, the budgets for these projects should be revised to recognize that the actual expenditures lag behind the budgeted amounts and it is necessary to reflect this lag in rates. When projects within the Fish and Wildlife program cannot ramp-up as quickly as expected, or for other reasons, BPA’s cost projections for the direct program will be inaccurate and will cause BPA to over-collect in rates for fish and wildlife expenses.

The members of NRU were chagrined earlier this year when BPA agreed to voluntary spring spill rather than relying on in-river transportation of migrating smolts in low water conditions. This had a negative effect on BPA's level of financial reserves, was inconsistent with the science supporting the Bi-Op, and according to NOAA Fisheries, will likely have an adverse impact on the survival of the smolts. Our understanding is that the IPR assumes on the revenue side that the Bi-Op will be implemented, including cutting off summer spill in August when the level of out migrating smolt falls below 300 fish per day. If the Federal Agencies fail to implement the best science contained in the Bi-Op, and extend summer spill into August when it is not needed by your Bi-Op's own standards, the BPA customers should not bear that financial consequence to BPA of foregone revenues from lost power generation. The foregone revenue should be replaced by cuts to the additional money going into the Fish and Wildlife Program, particularly for softer areas such as "research and evaluation." Given current market conditions, we assume that continuing summer spill beyond August 1st, when it is not needed to help fish migration, will cost about \$15 M (plus or minus \$5 M) in foregone revenues, which is equal to about a ¼ mill increase in power rates, or 0.8% on a base of \$28.77 mills/kWh. Rather than increasing rates, BPA should accept all or a portion of the \$13.2 M in reductions contained on page 15 of the IPR Fish and Wildlife costs as needed to offset foregone revenues tied to summer spill beyond the Bi-Op trigger. There is little information in the IPR documents to demonstrate conclusively that this money will be spent.

BPA should set an overall budget cap on the Direct Fish and Wildlife Program expenditures for the duration of the Bi-Op. Such a cap will require BPA and the Council to reduce expenditures in Research, Monitoring and Evaluation (RM&E) in order to fund new project proposals. This will set clear program expectations and send a strong signal to program managers that they must prioritize RM&E costs. It should make the program more efficient and effective, by hopefully spending ratepayer funds in ways that result in real improvements in fish and wildlife productivity and survival. To help implement the cap, any non-Accord projects that fail science review should not be funded.

BPA should encourage the Council to use the Independent Economic Analysis Board (IEAB) to a greater degree. The Council recently evaluated the value of the IEAB and determined that the IEAB is being underutilized. The IEAB can provide useful insight as to the relative cost-effectiveness of the program and the value of the FCRPS at large. The IEAB may be of particular value with respect to prioritization of RM&E projects. BPA should specifically request that the Council task the IEAB with a "big picture" cost/benefit review of projects in the program.

### **Agency Services**

NRU appreciates the consideration BPA staff gave to the detailed comments we provided on June 11<sup>th</sup> regarding the proposed FY 2012 – FY 2013 budgets for the Departments that are part of Agency Services. BPA has identified in aggregate about \$22.6 M in reductions per year in the draft IPR

compared to the initial IPR. We agree with all of the reductions the Agency made and would encourage you to continue looking for savings, even though the Agency Services budget is not a major driver in the overall size of a potential wholesale power rate increase for FY 2012 – FY 2013.

In examining spending levels, we strongly continue to believe that the appropriate base of comparison should be the level of spending in current rates (FY 2011) or \$256 M, compared to the proposed level of spending for FY 2012 – FY 2013. In that regard, the initial IPR budget averaged for the two year period showed an increase of 17.4% compared to the 2011 rate case expenses shown in the May 25<sup>th</sup> BPA handout. With the reductions in the draft IPR, these expenses of now about \$277 M are an increase of 8.1%, a considerable improvement from a total cost perspective. The large majority of the reduction is attributable to the elimination of the newly proposed catastrophic insurance policy.

When considering the impacts of inflation, and recognizing that the activities of Agency Services support are partially funded by Transmission Services, which is adding new requirements for central assistance, it is difficult for our staff to zero in on additional specific proposed activities that should be cut. Hopefully in the future BPA will undertake an IPR process where budgets funded from existing rates become the baseline of comparison for the next rate period, and increments for new activities are added on a prioritized basis that can be shared with the public. We believe that would create more meaningful dialogue between the Agency and customers rather than having the customers try to chip away at a new proposed spending level that does not seem integrally linked to the current revenue base.

In this overall context, we would like to see another \$4 - 5 M reduction in the Agency Services budget, which would reduce the overall increase to the 6 - 7% range. We do not have specific line item reductions to propose at this time, but if the Agency wants to achieve that objective of further reductions, we are willing to put in the time to formulate additional suggestions. Our assumption is that this would reduce expenses allocated to power rates by \$3.0 M.

### **Renewable Resources Program**

BPA is continuing to propose to include \$4M/year in the Renewable Resource Program for “Resource Development.” This appears to be a placeholder to collect money from ratepayers *just in case* BPA needs money for any variety of reasons, such as “resource studies, generation options, generation input purchases, resource purchase.” When NRU asked for further elaboration on what BPA intends to spend this money on, BPA replied that the \$4M/year would allow “Power Services to react quickly to changes in capacity needs occurring during the rate period. These capacity needs could be required for Tier 1 load, generation inputs or to support Resource Support Services. This budget could also be used for a BPA Tier 1 renewable purchase resource (to the extent that it exceeded the forecast augmentation cost in the rate case).”

NRU remains unconvinced that it is appropriate or reasonable to include this \$4M/year in BPA's budget for several reasons. First, BPA has not identified a specific need to acquire capacity in its draft Resource Program. Additionally, in various rate case workshops BPA has indicated that if they do need to acquire capacity during the rate period, it will be short-term acquisitions but more than likely BPA would use other means to manage capacity constraints on their system during the 2012-13 rate period. Second, if BPA does need to acquire capacity resources, then these costs should be allocated to the party requiring capacity acquisitions under the principle of cost causation. NRU would expect that the revenue recovered from the wind integration charge, demand rate and resource support service charges would be adequate to purchase any needed capacity. If BPA believes it will not sufficiently recover enough revenue from those charges to provide those services and therefore will need \$4M/year in the bank "just in case," then BPA needs to indicate which rate will recover this \$4M/year (i.e., if capacity is acquired to integrate wind, this cost should be allocated to and recovered from the wind integration charge). Third, in a rate case workshop, BPA stated the number and type of non-federal resources that will be using resource support services in the 2012-2013 rate period—this sums to about 7 aMW and includes one wind project, two landfill gas projects, one biomass project and one hydro project. NRU finds it hard to imagine that BPA will need to acquire even a portion of \$4M/year worth of capacity support for these resources. Fourth, BPA has also stated in a rate case workshop that they forecast the need for Tier 1 augmentation to be zero. This means there will be no need for money to fund any potentially renewable aspect of an augmentation resource.

Given lack of a sound business reason to collect \$4M/year, coupled with the poor state of the economy and the necessity for BPA to mitigate any potential rate increase, NRU recommends that BPA remove this \$4M/year Resource Development line item from the Renewable Resources Program. Further, given that BPA is operating under two year rate periods, should the need arise for capacity acquisitions, BPA will be able to add this to the FY 2014-15 budget.

### **Energy Efficiency Program**

NRU supports the capitalization of the energy efficiency acquisitions. NRU encourages BPA to use the most reasonable estimate of the expected life of the conservation measures planned to be acquired in 2012-13 as the basis of the amortization period. In addition, NRU suggests BPA reconsiders the ability to achieve planned levels of conservation in 2012-13 in light of the lack of an economic recovery. Both the BPA Energy Efficiency Action Plan and the Council's Sixth Power Plan make certain assumptions related to load growth (i.e., perhaps due to new housing starts) and economic growth or recovery. It seems reasonable that BPA (perhaps working in conjunction with the Council) reevaluate the assumptions made and determine whether the level of annual planned conservation in 2012-13 needs to be changed. If BPA determines ramp rates or other factors have changed, these changes should be taken into account when establishing both the expense and capital budgets.

## **Transmission Expenses**

It is important that BPA Transmission ensure there is sufficient staffing to efficiently perform in key areas, such as policy and rates, NERC Reliability Standards compliance and operations. There needs to be continuity in staffing and preservation of expertise in order to enable Transmission (and the customers) to move forward on pressing issues rather than spend time re-training staff.

We stress that there needs to be continuity in staff working on NT policy development. It is vitally important that Transmission develop policies that enable it to meet its Tariff obligation to provide load growth service for NT customers and to implement the goals of enabling non-federal resource development per the Regional Dialogue policy. In addition, there needs to be sufficient staff to ensure a coordinated approach to NERC standard compliance, between BPA and the customers. We appreciate the good work that is being done by Transmission staff, but fear human resources are being spread too thin.

### **Overview of NRU Reductions Compared to Initial IPR and BPA Draft Close Out letter**

Current Wholesale Power Rate for FY 2010 – 2011 = \$28.77 MWh.

Proposal	Adjustment Factor	Net Change In Expense	Cost Contribution to Rate Increase*
Initial BPA IPR	\$65 M = \$1.00 MWh	\$261 M	14.0%
Draft BPA Close Out	\$65 M = \$1.00 MWh	\$135.5 M	7.2%
NRU Reductions	\$65 M = \$1.00 MWh	\$78.5 M	4.2%

\*Does not include adjustment in wholesale power rates associated with forecast non-firm revenue earnings, IOU and DSI benefits or Planned Net Revenues for Risk. Only includes costs tied to higher level of expenses.

### **Summary of NRU Reductions in Net Expenses Related to Wholesale Power Rates Using Draft BPA Close Out letter as a Base**

(Initial reductions NRU proposed that BPA accepted in Draft Close Out letter of July 9, 2010 are not repeated in this document).

<b><u>Item</u></b>	<b><u>Amount</u></b>	<b><u>Impact</u></b>
Energy Northwest	\$20 M	Further reductions in fuel cost
Fish and Wildlife	\$13 M	Properly paced implementation of Bi-Op Fish Accords

Corps/Bureau	\$2 M	Reduce Cultural Resources Budget growth by half
Corps/Bureau	\$5 M	1.5% reduction in overall O&M budgets
Corps/Bureau	\$10 M	Capitalize rather than expense "betterments"
Agency Services	\$3 M	Power Services portion of further reductions
<u>Renewable Resources</u>	<u>\$4 M</u>	<u>Remove unspecified "resource development" costs</u>
Total reductions	\$57 M	

**Conclusion**

Thank you again for the opportunity to comment, and for all of the time you and your staff have dedicated to the IPR process. While some of the pressures for a rate increase are beyond the Agency's control, we believe the above recommendations will further mitigate the impact, are achievable consistent with sound business practices, and will continue the good will between the Agency and its customer base.

Respectfully,



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