

Prepayment Funding Option Summary of Questions from Customer Comments

The Desert Southwest Region (DSW) is posting the letters received on this topic. As can be seen from a review of those letters, widespread support for using prepayments for construction activities was received. DSW did not receive any letters opposed to moving forward with making use of available prepayment dollars to assist in addressing unfunded construction needs. DSW intends to continue to a collaborative process with its customers in its further pursuit of the goal of addressing infrastructure needs while utilizing cost-effective approaches. This document addresses particular questions within the comments DSW received.

1. Question: How does DSW propose to use the \$15 million of prepayments that are currently available?

Response: Although DSW is proposing to use available prepayments for construction, at this time we are not proposing specific projects to be funded by prepayments. DSW anticipates that the selection of projects will be a collaborative process with the customers that will occur at a subsequent meeting(s). As DSW mentioned during the customer meeting, the \$15 million figure should not be viewed as the definitive quantity. It was provided to give a general quantitative feel.

2. Question: Was this \$15 million intended for annual or capital costs?

Response: This is the accumulated amount of unused Parker-Davis Project (P-DP) prepayments from fiscal year 2009. That amount had not been specifically intended for either annual or capital costs. If we had not determined that it was appropriate to use the cash for construction purposes, it would have to be sent to Treasury.

3. Request: Please list the construction projects in the Ten-Year Plan that would be funded through appropriations, Transmission Infrastructure Program (TIP) and prepayments. Identify the potential rate impacts of each funding source.

Response: During the customer meeting held on February 17, 2010, DSW presented that its first preference for funding construction will continue to be appropriations. For projects eligible for TIP and for which customers support TIP funding, TIP funding would be used as the next alternative. Funds available from prepayments would then be used to help bridge the remaining gap between construction needs and funds available to address those needs. Construction funded through appropriations and through prepayments impact the rates exactly the same. At this time, DSW is not proposing any funding mechanism for specific projects in the Ten-Year Plan.

4. Question: Will the use of prepayments be limited to the power system from which they originated? Limited to DSW power systems?

Response: DSW believes that prepayments within the Region will provide beneficial funding for DSW construction projects. The revenues and expenses of each Federal Power Project (Project) shall be maintained separate and distinct. This is accomplished through the financial reporting process, the results of which are included in the Power Repayment Study (PRS) thus ensuring that revenues and costs for each project match within each PRS. However, the cash available after accounting for each Project's revenues and expenses will be utilized for Region-wide purposes because cash is not a project-specific commodity. Specifically, Intertie and P-DP currently receive customer prepayments for firm point-to-point transmission service. The revenue requirements are set for each project in each respective PRS to assure that project costs are recovered. Managing cash, however, is done on a Region-wide basis. Since the majority of the aging infrastructure challenges are on the P-DP but the vast majority of cash available is not generated from P-DP transmission bills, making effective use of customer prepayments to address the Region's construction challenges will require using cash between Projects. Therefore, DSW intends to make the use of prepayments from other power systems an element of a collaborative construction planning process with our customers.

5. Question: Please distinguish the use of prepayments for construction from that of a revolving fund.

Response: Unlike a revolving fund, the use of prepayments will not allow DSW to access its own receipts to build a pool of funds to be used for an undetermined future purpose. Prepayments are customer advances, and will be sent to Treasury if they are not designated for specific purposes. Some customers have advocated for DSW accumulating dollars over the long term to be ready to respond to infrastructure needs. While a revolving fund would provide authority to do so, customer advances do not provide for this capability.

6. Question: If prepayments are used to fund capital assets, should those assets be excluded from the PRS since they are prepaid?

Response: Customer prepayments are limited to those amounts required to generate adequate revenue to repay all project costs. Customers would not be asked to advance fund any capital assets or amounts outside of the rate. As construction projects are completed, the capitalized assets will be amortized and included in the rate, as it is now with construction projects that are funded with appropriations. Including the

assets in the PRS will not result in the customers paying twice for the same asset, since the customers are not funding capital assets outside of the rate.

7. Question: Is DSW willing to negotiate an agreement similar to the Parker-Davis Project Advancement of Funds arrangement? If not, please describe why such an agreement would not be suitable to implement the use of prepayments for construction.

Response: DSW recognizes customer concerns regarding oversight and is considering all options, including options similar to the Advancement of Funds process, to alleviate those concerns.

8. Question: How could the Joint Planning Agreement (JPA) be modified to ensure that customers will be a part of the decision process for the use of prepayments?

Response: The JPA provides for an interactive planning forum and process in which DSW and the customers identify transmission concerns, prepare joint transmission plans and review and reach general agreement about capital improvements and replacements. Although the JPA process already affords significant customer input, it could be strengthened with more frequent meetings and additional coordination regarding capital improvements and replacements. Customers' suggestions on improvements will also be considered.