Department of Energy
Western Area Power Administration
P.O. Box 281213
Lakewood, CO 80228-8213

NOV 1 0 2005

Dear Parker-Davis Project Firm Electric Service Customers:

A meeting was held on August 5, 2005, to discuss the proposed Parker-Davis Project (P-DP) contract extension prototype Amendment No. 1. During that same meeting, there was also a lengthy discussion about the "Opt-In-Program" proposal. After the meeting, Western sent out a letter dated August 5, 2005 requesting that each P-DP customer indicate their preference with regard to the Opt-In Program. The two alternatives were as listed below:

- Continue with the existing status quo P-DP contract where the energy delivery obligation is fixed and firming purchases are included in the rate; or
- Adopt the Opt-In-Program which allows for an annual reduction in the contract energy delivery obligations based on projected hydrology conditions in lieu of making rate-based power purchases.

Subsequent to this meeting, Western sent out additional analysis, had several conference calls, and attended meetings with customers to provide additional data for customers to consider in their decision making process. The comments are summarized below:

- A comment was received that the "Opt-In" name is too confusing and suggested that the name "Purchase Option Program" be adopted. Western agrees with this comment. All future correspondence and discussion will refer to the "Purchase Option Program."
- Most comments expressed strong support for retaining the status quo, citing that the existing contract provides assured delivery of a set quantity of energy, the certainty of rate stability, and less risk exposure to volatile spot market prices and the resulting potential cash flow problems if market prices spike.
- Comments were also received supporting the Purchase Option Program, primarily from customers who have their own generation resources, have the ability to purchase power at less than market prices, and have established risk mitigation organizations, equipment and procedures.

Western also received inquiry as to whether or not it would be possible to make both options available, rather than requiring that all customers accept one option or the other. Western has evaluated this request and feels that offering each P-DP customers the opportunity to select either their existing status quo contract, or a contract with purchase option language can be accommodated. The key characteristics of this blended approach follows:

- Each customer must select either the status quo or the purchase option language for inclusion in their P-DP contract extension amendment. For those that select the purchase option, the contract language will be as shown in enclosure 1.
- For those P-DP customers that select status quo, the energy delivery obligation will be fixed.
- For those P-DP customers that select purchase option, the annual process for determining the energy delivery reduction will be similar to that which was described in Western's April 13, 2005 letter and the August 5, 2005 meeting. The difference is that the energy reduction applies to purchase option customers only. All other parts of the process apply to all P-DP firm electric service customers. The Purchase Option Program process is described in enclosure 2.
- All firming purchases will be included in the rate and there will be one rate for all P-DP firm electric service customers.

Western is prepared to send out an executable contract extension amendment to each P-DP customer as soon as we received notification with regard to the language (status quo or purchase option) you would like to have included in your contract. If you would like to include the Purchase Option Program language in your contract extension amendment please let us know no later than November 30, 2005.

If requested, Western is available for individual discussion or group meetings. If you have questions, comments, or would like to have further discussion, please contact either Jean Gray at (602) 605-2555 or Penny Casey at (602)-605-2585.

Sincerely

Jean Gray

Jean Gray
Assistant Regional Manager
for Power Marketing

2 Enclosures:
Purchase Option Program Contract Language
Parker-Davis Project Firm Electric Service Purchase Option Program Process

Purchase Option Program
Contract Language

The following additional language will be included in the customer's Parker Davis Firm Electric Service Contract Amendment No. 1 if the customer chooses the "Purchase Option Program":

[Note: Section numbers are approximate]

5. **MODIFICATION OF SECTION [4] OF THE ORIGINAL CONTRACT (DEFINITIONS)**: Subsection [4.6] of Section [4] of the Original Contract is deleted in its entirety and replaced by the following:

> "[4.6] Seasonal Energy is the maximum quantity of firm energy expressed in kWh that Western is committed to supply and the Contractor is entitled to receive each Winter Season and each Summer Season pursuant to subsection [5.1.2] herein."

6. **MODIFICATION OF SECTION [5] OF THE ORIGINAL CONTRACT (FIRM ELECTRIC SERVICE)**: Section [5] of the Original Contract is amended in the following manner:

....

6.2 Subsection [5.2] of Section [5] of the Original Contract is deleted in its entirety and replaced by the following:

> "[5.2] Monthly Energy Obligations: Western's Monthly Energy obligations to the Contractor shall be set forth in Exhibit A, attached hereto. Monthly Energy quantities may be adjusted annually based on projected hydrology conditions. The Contractor may request Western to purchase energy on a pass through cost basis to supplement the firm electric service resource. Such pass through cost purchases shall be set forth in a separate agreement between the Parties. Deliveries in any monthly billing period shall not exceed the Monthly Energy obligation established for that month, except as otherwise agreed between the Parties in writing. The Monthly Energy obligations may be increased from time to time at Western's discretion, if short-term conditions allow. If the Monthly Energy obligation is increased for any month, it will revert in subsequent months to the Monthly Energy obligation as set forth in Exhibit A, unless the Contracting Officer notifies the Contractor in writing. The Contractor may not transfer energy from month to month without revision to Exhibit A."

Parker-Davis Project Firm Electric Service Purchase Option Program Process

The purpose of this document is to describe the annual process that will be used to adjust energy delivery quantities based on projected hydrological conditions for those Parker-Davis Project (P-DP) Firm Electric Service (FES) customers that have selected Purchase Option Program contract language. What follows is a hypothetical scenario to demonstrate how this Purchase Option Program process will work.

- Assume that there are five customers who select the Purchase Option Program language for their contract and their total P-DP FES Contractual Energy Obligation totals 1000 GWhs:

Customer	Annual Energy Delivery Obligation
A	200 GWhs
B	200 GWhs
C	200 GWhs
D	200 GWhs
E	200 GWhs
TOTAL	**1000 GWhs**

- Assume that the annual estimate for P-DP generation during the upcoming year is 10% below the total contractual obligations of all FES customers.
- Under the Purchase Option Program, the energy delivery obligation for each of the five Purchase Option customers would be adjusted proportionately by 10%. Thereafter, each of these customers would have the option to have Western purchase power for them on a pass-through-cost basis up to the energy delivery level of their contract.

Yearly estimate of P-DP generation:
= 10% adjustment
= 20 GWhs reduction to each customer

Customer	Adjusted Annual Energy Delivery Obligation
A	180 GWhs
B	180 GWhs
C	180 GWhs
D	180 GWhs
E	180 GWhs
TOTAL	**900 GWhs**

- After the adjustment, the total energy delivery obligation for these customers for this annual season would be 900 GWhs.

- Assume that under the Purchase Option Program, Customers C, D, and E exercise the option for Western to purchase power for them. As a result, Western would make purchases of 60 GWhs on a pass-through-cost basis plus transaction fees to provide the service for Customers C, D, and E.

- The cost of 60 GWhs @ $50/MWh = $3,000,000, which would be passed through to customers C, D, and E.

- Customers C, D, and E would advance $3,000,000 plus transaction fees to Western prior to power being purchased. The money would be deposited into a trust account for each customer who elects to have Western purchase energy on their behalf.

- Based on the actual cost of the power purchases, there would be provision for customers to provide additional funds, if necessary, and provision for an after-the-fact accounting and true-up.

During the annual operating year, the actual generation will most likely be different than the estimated generation which was formulated prior to the beginning of the year. The actual generation compared to the estimate would be treated as follows:

- If the actual P-DP generation shortfall is greater than 10%, then there will be rate based purchases in order to meet contractual obligations to all P-DP FES customers.

- If the actual P-DP generation shortfall is less 10%, then the extra energy would be disposed of as it is today. That is:

    1. Issue excess energy to all P-DP FES Customers;
    2. Make deposits to energy banks; and/or
    3. Make surplus energy sales and deposit the revenue into the Generation Trust Account established under the P-DP Generation Facilities Advancement of Funds Contract.

On a going forward basis, the energy bank balances will be used as they are today. That is, the energy bank balances will be taken into consideration for meeting contractual obligations when formulating the annual operating plan. Energy bank balances will be considered before making the annual adjustment to energy delivery contractual obligations for Purchase Option customers. The energy bank balances would also be used to offset purchases if the actual generation is less than the adjusted contractual obligation.

The Central Arizona Project surcharge would not be assessed to the supplemental pass-through-cost power that is purchased for those Customers participating in the Purchase Option Program.