

February 28, 2007

AIDEA AND AEA RESPONSES TO QUESTIONS FROM DCCED
FINANCE SUBCOMMITTEE

Below are AIDEA and AEA's responses to the February 12, 2007 AIDEA Questions from the DCCED Finance Subcommittee.

The questions use "AIDEA" to represent both AIDEA and AEA; the responses do not.

Ketchikan Shipyard

Regarding the Ketchikan Shipyard, Representative Chenault, Co-chair of House Finance, requests answers to the following questions (please copy him with your response):

1. What is the total amount of State funds spent to date? **See attached spreadsheet.**
2. What is the total amount of Federal funds spent to date? **See attached spreadsheet.**
3. What is the total revenue that has been received by year? **See attached spreadsheet.** Please provide a 10 year revenue projection. **The shipyard operator is currently working on revenue projections, but considers this to be proprietary information, the disclosure of which could adversely impact their operations.**

T-line between Teeland and Douglas Substation

1. Regarding the \$20.3 million legislative appropriation in 2002 to build the bypass line from Teeland Substation to Douglas Substation, why after 5 years has AIDEA failed to complete, or to even begin construction of the line?

The most significant cause for the delays on this project arose as a consequence of AEA attempts to work cooperatively with the IOC Utilities on the project. AEA and the IOC Utilities agreed that significant cost savings could be achieved if the Utilities assumed greater control over this bypass project, particularly in conjunction with Utility commitments to address long neglected major maintenance items, and address snow-load issues. See, e.g., April 22, 2004 letter from Ron Miller to Senator Therriault.

Municipal Light and Power (ML&P), an Anchorage utility, agreed to manage the design and construction of the bypass line. The Alaska Intertie Operating Committee (IOC) supported this approach. See attached copy of the IOC minutes dated May 18, 2004, describing three resolutions in which the IOC accepts (1) early route study report, (2) recommendation of the MEA parallel route, and (3) recommendation that ML&P perform the duties of project manager.

AEA and ML&P began negotiating a project management agreement. ML&P objected to AEA's initial September 2004 draft of the Project Management Agreement, expressing their belief that AEA under the draft maintained too much oversight of the Project. This initial approach was abandoned in early 2005, and AEA agreed to provide less project oversight. AEA and ML&P continued negotiating a project management agreement, leading to the final August 2006 version of this agreement, a copy of which is attached.

Under the agreement, ML&P will determine the schedule for design and construction of this intertie extension. Before the August 2006 agreement can become effective, ML&P must have the agreement approved by the Anchorage Municipal Assembly. AEA continues to wait for ML&P to take the agreement to the Anchorage Municipal Assembly for approval.

Another cause for delay on the project arose because IOC Utilities disagreed amongst themselves regarding prioritizing the use of these appropriated funds. MEA suggested that these funds should be used for repairs and other purposes such as snow load mitigation. GVEA, ML&P and CEA (the Utilities) requested that the initial 5-miles of the Alaska Intertie route be included as part of the bypass project. The Utilities suggested that this section needed to be part of the bypass project because it is owned by MEA and used under a contract with a term that ends in 2018. However, the use of this 5-mile section in conjunction with the Alaska Intertie is not in jeopardy of being lost since the contract with MEA provides for perpetual use of the line even after the contract term ends. The Utilities still contend that this section still needs to be part of the bypass project because it is inadequate for 230kv operation.

AEA has maintained that the legislature intended for this appropriation to first be used to construct a line to bypass the MEA-TLS – approximately 19 miles of MEA owned line which is no longer used under the Alaska Intertie Agreement, but rather is used by the Utilities and the City of Seward utility under an RCA order. *See, e.g.,* April 22, 2004 letter from Ron Miller to Senator Therriault.

Despite delays, progress has been achieved. Dryden & LaRue, Inc. was hired to prepare a feasibility level assessment of several route options for the Project. *See* January 2004 analysis, a copy of which is attached. IOC utilities requested additional analysis be conducted to help determine the preferred route.

2. When will construction begin? Completion date?

The Anchorage Municipal Assembly must approve the AEA/ML&P Project Management Agreement and ML&P must appoint a project manager for work to begin.

3. Will AIDEA bear any cost growth due to delays, or are sufficient funds available including accrued interest to complete the line?

Interest from the \$20.3 million was not appropriated to the Project. Interest remains with the Railbelt Energy Fund. Under the AEA/ML&P Project Management Agreement, ML&P is required to notify AEA of any funding shortfall. Prior to proceeding to the construction phase of the Project, written agreements must be in place to guarantee funding overruns. In order to contain the cost of the project to the appropriated amount, AEA suggests that ML&P at the time of design and upon completion of a detailed construction cost estimate establish viable alternates, either additive or deductive, that will allow the project to be completed within the existing funding. In the alternative, AEA would work with the utilities if they elect to seek financing, or elect to cover shortfalls with internal utility capital funding. AEA expects that ML&P would bring this information back to the IOC prior to construction.

T-line between Douglas Substation and Stevens Substation

Regarding the September 26, 2005 letter signed by AIDEA and three of the six electric utilities in the Railbelt, and specifically referring to the proposed \$14 million 115kV transmission line between Douglas and Stevens substations, please provide the following information:

1. The proposed 115Kv line would only serve the remote Stevens Substation owned by the local utility and connected to the Alaska Intertie. Although Stevens is connected to the Railbelt power grid, the substation is idle - perhaps because of slower-than-expected load growth or alternate service being available through local distribution lines. The local utility has waged an expensive television campaign criticizing AIDEA for alleged safety concerns in this area caused by differential snow loading on the Douglas-to-Stevens section of AIDEA's Alaska Intertie which connects Anchorage and Fairbanks. Why would AIDEA consider spending public funds to run a second line from Douglas to Stevens without seizing the one-time opportunity to use the new line, which would parallel the "snow load" portion of the Alaska Intertie, to solve the snow loading problem identified in the utility's advertising campaign?

This solution is supported by expert electrical transmission engineers and can be accomplished at very little cost. It would increase the reliability of power exchanges between Anchorage and Fairbanks, eliminate the snow loading safety concerns and save AIDEA millions to rebuild the snow load section as a separate project. Please provide your engineers' assessment justifying building the line to operate at 115kV in isolation from AIDEA's Alaska Intertie, instead of at 138kv or 230kv to be operated as part of, and in parallel with AIDEA's Alaska Intertie.

The Alaska Energy Authority understands that this question addresses two different projects, with different goals, and that would serve and benefit two different groups of railbelt ratepayers. The MEA proposed 115kv line would serve

ratepayers of the local utility, MEA, and would be integrated into MEA's distribution system. The GVEA proposed 230kv (or 138kv) line purportedly would be integrated into the Alaska Intertie and would primarily serve ratepayers who receive power transmitted over the Alaska Intertie – GVEA customers; and secondarily serve ratepayers of utilities that sell power transmitted over the Alaska Intertie – Chugach and ML&P.

Comparison of the two projects is therefore an apples to oranges comparison – any conclusion depends more upon what goals, benefits, or particular railbelt ratepayers interests are intended to be promoted. At this time, AEA does not advocate for either proposed project, and particularly does not advocate for one project over the other.

AEA is unaware of any engineering analysis to support either project. AEA is unaware of any cost projection for either project. AEA is uncertain whether MEA's proposal would have provided full or only partial funding for that project.

AEA is uncertain, but is skeptical, that a cost projection on MEA's 115kv proposed line would support GVEA's proposed 230kv (or 138kv) proposed project. AEA is unaware of the basis for the statement “[t]his solution is supported by expert electrical transmission engineers and can be accomplished at very little cost.”

AEA is uncertain as to why GVEA would propose a 138kv project in any event. One of the stated purposes for the current bypass project is to upgrade the Alaska Intertie to 230kv capability. GVEA's proposal to build a 138kv project would appear to have a limited useful life, and promote a questionable cost-benefit economic value.

AEA is unaware of any engineer's study or cost-benefit analysis supporting the construction of a parallel, redundant line to cure snow load issues. While MEA commenced a “television campaign” regarding snow load safety issues a few months after the September 26, 2005, letter referenced in the question, AEA is not aware of any other IOC utility that believes an actual snow load safety problem exists, nor any other IOC utility that believes construction of a redundant, parallel line could be justified under any cost-benefit analysis as a solution to snow load issues.

AEA has worked cooperatively with the Intertie Operating Committee to find ways of safely operating the Intertie under snow load conditions. A solution has emerged that appears to promote a public interest: cost-benefit analysis. ML&P is the operator of the portion of the Alaska Intertie subject to snow load issues. ML&P has a responsibility to monitor snow load conditions, and de-energize the line if unsafe conditions exist. To assist ML&P, a snow-load monitoring system has been installed. This is an automatic reporting program from conductor-tower mounted snow load monitors that reports any adverse loadings. To further assist ML&P,

anytime there are recorded snow events, a ground based snow machine patrol is sent out to confirm the intertie conductors are not sagging.

In practice, the monitors appear to have proven reliable, and patrols appear to have been effective in assuring safe operation. There has been no documented serious snow loading on the line segment for the last decade.

AEA and the IOC hired engineers with expertise in transmission line safety to review the current intertie operations in order to confirm that this approach to snow-loading is safe and in the public interest. One of the conclusions of the study is that the line is being operated safely. A copy of the report is attached. AEA has not heard any IOC Utility (other than MEA) disagree with, or object to, the conclusions of the report.

2. The local utility recently attempted (until they were halted by RCA) to shut down the Alaska Intertie connecting Anchorage and Fairbanks. Assuming the proposed Douglas-to-Stevens line will be part of, and operated in parallel with AIDEA's Alaska Intertie, why would AIDEA propose to publicly fund the line and then transfer ownership to this non-generating local utility?
Shouldn't AIDEA retain ownership, or better yet transfer construction responsibility, title and risk to a joint action agency comprised of the utilities responsible for electric generation and power system dispatch and operation in the Railbelt?

AEA, offering its assistance to RCA in an attempt to help resolve disputes between IOC utilities, participated in RCA-ordered mediation and in the RCA hearings referenced in the question. In the course of that participation, AEA heard MEA represent to other IOC utilities and to the RCA that they did not seek to "shut down" the Alaska Intertie, but rather primarily sought to reduce the operating voltage of the MEA-TLS from 138kv to 115kv.

AEA understands that MEA would intend to own its proposed 115kv project, and that it would not be "part of, and operated in parallel with" the Alaska Intertie. AEA has no intention to own MEA's proposed 115kv project, and, therefore, would not "transfer ownership" to MEA.

Has AIDEA given notice to the utilities to "cancel the Alaska Intertie Agreement"? If so, why?

AEA's October 16, 2006 letter providing notice of intent to terminate the Alaska Intertie Agreement (effective October 16, 2010) with the reasons stated therein is attached. The April 22, 2004 letter from Ron Miller to Senator Therriault, a copy of which is attached, describe unfulfilled IOC Utility commitments to address neglected major maintenance items, and further reflects reasons why AEA gave notice of termination.

Has AIDEA received an offer to purchase the Alaska Intertie, or engaged in discussions regarding potential purchase by any utility or consortium?

At the December 1, 2006 AEA Board meeting, MEA presented the attached proposal to purchase the Alaska Intertie, "... for approximately \$50 million, under terms and conditions mutually agreeable to ..." AEA. At that meeting, MEA presented to AEA a sealed envelope containing what was described as confidential terms of the offer to purchase. The AEA Board directed staff to conduct a public process to consider what should be done with the Intertie, including whether the Intertie should be sold, and if so, to whom. This could entail an RFP or other public disposal process and for that reason, the sealed envelope from MEA was returned unopened to the utility on December 1, 2006, since acceptance could have tainted any request for proposal or other public disposal process.

AEA is currently working through a public process of considering whether there should be unified systems operation for the management and dispatch of electric power in the Railbelt. This work was funded with an appropriation of \$800,000 by the 24th Legislature. A potential disposition of the Alaska Intertie by AEA is one of the items to be addressed during these public meetings.

AEA is not engaged in any discussions regarding potential purchase of the Alaska Intertie by any utility or consortium.

Regarding the balance of the Railbelt projects identified in the September 26, 2005 letter mentioned above, please provide the individual cost/benefit analyses for the projects and identify any matching funds or utility debt to be joined with public dollars, as was done when funding previous Railbelt projects.

AEA does not have a cost benefit analysis of the projects, nor does AEA take any position on the projects that were proposed to be funded during the second session of the 24th Legislature. The back up that was submitted to the legislature and to OMB is attached.

Healy Clean Coal Plant

Please provide a report identifying total AIDEA spending on HCCP from all internal and external funds, regardless of source, for all direct and indirect construction, operating, maintenance and other (administration, legal, consulting, etc.) activities from project inception to date. Please identify any debt, including write-downs or write-offs and any revenue generated to date.

See attached spreadsheet.

Of the AIDEA costs reported in the spreadsheet, AIDEA estimates it incurred more than \$15 million of expenses for the benefit of GVEA's Unit 1. It also paid GVEA \$1 million for development of HCCP as part of the 2000 Settlement Agreement, and

has paid GVEA more than \$5 million for custodial duties, heat and electricity since HCCP ceased operations in 1999.

Information requests concerning the period between now and 2014 when Homer proposes to buy power from HCCP:

1. HCCP was shut down in 2000 following failed performance tests, funds exhaustion, major component failure and explosion events that rendered the plant unsafe for employees. It has sat idle since. Please provide your engineers' scope, schedule and budget regarding the Agency's intention to accept the risk and to provide the funds to permit, convert, complete, start-up and operate HCCP. Provide fund sources, engineers' reports and cost-benefit estimates.

AIDEA disagrees with these characterizations of HCCP. In 2000, HCCP did not suffer from "funds exhaustion, major component failure, and explosion events that rendered the plant unsafe for employees." Nor did it fail performance tests.

AIDEA and nationally recognized engineers who have evaluated HCCP operations, or who have inspected the plant, believe that it is safe, reliable, and capable of operating according to design specifications.

The results and the history of HCCP's Date of Commercial Operations test supports AIDEA's views that HCCP did not fail its "performance tests." The 1991 Power Sales Agreement between GVEA and AIDEA required that by January 1, 2000 HCCP meet the performance standards for determining the "Date of Commercial Operations." Although construction of HCCP was delayed for several years owing to permitting and construction problems, the contractual deadline for HCCP's "Date of Commercial Operations" remained as agreed upon in 1991. Therefore, following completion of construction, AIDEA was required to conduct HCCP operational tests sooner than was contemplated by both GVEA and AIDEA when the Power Sales Agreement was entered into. This required AIDEA to perform the Date of Commercial Operations test well before AIDEA's engineers had the expected opportunities to fine-tune HCCP's systems.

After HCCP was placed into operation, AIDEA and GVEA jointly selected Dennis Swann, an engineer with a nationally recognized reputation and experience with coal generation plants, to act as the Independent Engineer for the purpose of determining whether HCCP satisfied the Date of Commercial Operations requirements.

The contractual requirements for the Date of Commercial Operations were:

- (l) "Date of Commercial Operation" means the date, which shall not occur before the end of the Test Period, on which engineers retained for this purpose by the Authority and acceptable to the Purchaser have (i) determined the Project has operated at not less than 50 megawatts, net of

station service, at a Capacity Factor of not less than 85 percent, for a period of 90 consecutive days, using coal with characteristics equivalent to those of long-term Usibelli coal, as defined in the Coal Supply Agreement between the Purchaser and Usibelli Coal Mine, Inc. dated January 1991, and (ii) stated that, as the result of their independent observations of the test operations of the Project and tests and inspections required by the engineers, the major systems of the Project are performing in accordance with design specifications and tolerances and that the engineers know of no reason why the Project will not perform on a sustained operating basis as provided under this Agreement if the Project is operated, maintained, and renewed according to standard utility practices.

Initially AIDEA and GVEA disagreed about the extent of these requirements, so Swann, as the Independent Engineer, was compelled to resolve the dispute, and determine what was required by these provisions. After the disputes were resolved, and at the conclusion of the test, Swann, as Independent Engineer, found that the “test results were inconclusive regarding the requirements set forth in the [1991] Power Sales Agreement.” He did not find that HCCP failed to function properly or that it did not perform as designed. He concluded that the test results were inconclusive in part because he found that the test was biased due to the fact that the quality of the coal used during the test was greater than was intended when the Power Sales Agreement was signed. He also found the test inconclusive because AIDEA had available a larger maintenance crew, including equipment manufacture representatives, than would normally be utilized during conventional operations. The excessive maintenance crew, Swann thought, was able to respond to equipment problems more rapidly than during normal operations and therefore it reduced HCCP’s down-time during test operations.

Even though Independent Engineer Swann did not find that HCCP conclusively passed the Date of Commercial Operations tests, AIDEA concluded that during the test period HCCP had demonstrated that with additional time for refining HCCP’s various systems, and with some limited modifications to them, it could perform economically on a sustained operating basis with the use of a slightly higher quality of coal. Swann’s report supported this view. His report said this about HCCP’s performance during the test period:

"It is our opinion that the major systems of the project are performing in accordance with design specifications and tolerances.

It is our opinion that the plant, as configured and if operated and maintained in accordance with standard utility practice, could be considered as a

commercial plant which is of comparable efficiency with similar plants if the coal delivered and burned remains above 7,200 btu/lb. Note that maintenance of the coal delivery system will be much higher than that of other coal burning facilities.

If HCCP were operated on ROM coal having a heat content in the range of 7,200 to 7,800+ btu/lb, we find no reason that the project will not perform on a sustained operating basis if operated and maintained in accordance with standard utility practices. We do note however, that the maintenance on the coal transport system from the feeder outlet to the combustor inlet will be higher than industry standards, thereby reducing capacity factors.”

With respect to the safety of HCCP, during a later deposition Swann expressed this opinion:

Q. All right. Well, Mr. Swann [the Independent Engineer], you spent a lot of time at this plant in the past couple years; have you not?

A. Yes, I have.

Q. In your view, based upon your observations over the past couple of years, is this plant safe?

A. Yes, it's as safe as any coal-fired power plant that I've been in.

Following the operational test periods, Swann also made the following observations regarding whether HCCP should be retrofitted to conventional low-NOx combustors, as GVEA has advocated:

"Retrofit Considerations. It is our opinion that conversion of the combustion equipment from the existing TRW precombustor/slagging combustor system to conventional low-NOx burners will not improve the commercial viability of HCCP.

....

Therefore, it seems that retrofitting low NOx burners on HCCP would be a step backward."

In light of the Independent Engineer's favorable comments about HCCP performance and his negative comments regarding retrofitting HCCP's combustors,

and based upon AIDEA's belief that limited modifications to HCCP would address HCCP's higher than industry standards maintenance costs, AIDEA requested additional time from GVEA to demonstrate HCCP's ability to satisfy the Date of Commercial Operation requirements.

GVEA promptly rejected AIDEA's request, and gave notice of termination of the 1991 Power Sales Agreement. After several months of negotiations, AIDEA and GVEA entered into a definitive Settlement Agreement dated March 8, 2000 ("Settlement Agreement").

Under the Settlement Agreement, GVEA was given the exclusive right to develop HCCP in any manner that it might choose, including a retrofit to conventional low-NOx combustors. AIDEA paid GVEA \$1 million up-front, and agreed to pay an additional \$4 million if GVEA elected to commit to develop HCCP. GVEA pursued development of HCCP until April 2, 2003, when it gave AIDEA notice that it was abandoning its efforts and was terminating the 1991 Power Sales Agreement.

After GVEA abandoned its efforts, the Settlement Agreement gave AIDEA the right to develop HCCP. AIDEA exercised this right, first by exploring options to develop HCCP with GVEA, including joint AIDEA/GVEA Board level efforts. These efforts, although extensive, were unsuccessful.

Subsequently, AIDEA undertook a public solicitation for entities interested in developing HCCP. A technical conference on HCCP conducted as part of the public solicitation was also held in December 2004. These efforts eventually led to a Power Sales Agreement and a Project Development Agreement between AIDEA and Homer Electric Association (HEA).

HEA hired engineers Shaw, Stone and Webster to evaluate HCCP's current condition and to propose improvements to bring it into operation. Shaw reported its findings in a March 28, 2006, report titled "HCCP Condition Assessment and Restart Study," a copy of which is provided. This report supported Dennis Swann's favorable conclusions regarding the ability of HCCP to be placed into operation without conversion to conventional low NOx combustors. The executive summary of that report contains the following conclusions:

SSW has completed the above referenced study. The primary results of this study as determined by SSW are:

- HCCP is in good condition and has incurred since 1999 no significant deterioration during the shutdown
- If recommendations for remediation and system separation are implemented, SSW knows of no reason why HCCP cannot be operated separately from Unit 1 in a safe and reliable manner for the duration of its

design life provided industry standard operation and maintenance activities are performed

- **SSW concurs with the HGI coal handling study with minor scope and cost adjustments.**

The basic provisions of the Power Sales Agreement and a Project Development Agreement between AIDEA and HEA include:

- a. HEA agrees to pay AIDEA (a) \$65,795,000, plus (b) the net restart and interim operation costs (AIDEA costs less revenues), with interest at 5.25%, amortized over the time HEA purchases power under the Power Sales Agreement (which is anticipated to commence January 1, 2014).**
- b. HEA agrees to be responsible for all HCCP generation and transmission operations, maintenance, and related issues when HEA begins purchasing HCCP power. HEA and AIDEA will have shared responsibility for these issues during earlier interim power sales.**
- c. HEA has the right to evaluate HCCP's operational performance for two years after commercial operations commence, at which time HEA may elect either to commit to the long-term power or to terminate the Power Sales Agreement.**
- d. The development of HCCP, and all related contractual obligations between HEA and AIDEA, are contingent upon AIDEA obtaining from GVEA, in the mediation or in the pending litigation, leasehold and other interests at the Healy site to enable HCCP to be placed in operation, consistent with the terms of the Settlement Agreement. In addition to providing for a ground lease, the Settlement Agreement provides:**

"The parties further agree to execute such agreements as are necessary and appropriate to provide AIDEA a full opportunity to maximize the economic utility of HCCP, recognizing GVEA's desire and necessity to retain the beneficial use of Healy #1."

AIDEA and GVEA are engaged in mediation attempting to negotiate a ground lease and other appropriate agreements.

The Shaw, Stone and Webster physical assessment report HEA commissioned also provides information regarding the estimated cost of placing HCCP into operation. AIDEA believes the cost of the restart project ultimately will exceed the approximate \$29.8 million reported in this study. The successful resolution of the current mediation between AIDEA and GVEA will require modifications to the HCCP development plans assumed in the Shaw, Stone and Webster report. These modifications are likely to increase the total estimated restart costs. AIDEA will

attempt its negotiations with GVEA to minimize modifications to development plans that would require cost increases.

2. What is the estimated power cost, sales price and profit/loss to AIDEA on a per kWh basis by year?

Under its agreements with HEA, AIDEA will not recognize any profit or loss during the interim power sales. Any profit or loss on interim power sales will decrease or increase the amount HEA pays AIDEA monthly when HEA begins purchasing the HCCP power.

AIDEA believes that the sales price for interim power sales will be a negotiated price, with the upper limit being the cost of the railbelt power that HCCP power would replace. HEA and AIDEA will exert joint efforts to negotiate interim power sales agreements. According to the terms of the agreements HEA, rather than AIDEA, will be the primary beneficiary of all power sales. AIDEA believes that the interim sales of HCCP power could significantly benefit both HEA and the purchasing railbelt utility because HCCP power should be available at a cost lower than the current cost of generating some railbelt power.

HEA has developed confidential, proprietary estimates of the power costs for interim power. Disclosure of this confidential, proprietary information would likely disadvantage HEA (the primary beneficiary of interim power sales) in any HEA/AIDEA negotiations with any power purchasers. It would therefore be inappropriate to disclose such confidential, proprietary estimated power costs at this time.

3. Please identify the purchasers of power from the plant, including purchase agreements and annual purchase quantities by year?

There are no current agreements for the purchase of interim HCCP power, and therefore no specifically identified power purchasers.

Sale of the power from HCCP will require its restart and placing it into operation. No realistic estimate of when that will occur can be made until after AIDEA obtains from GVEA the necessary rights related to the Healy site, consistent with the Settlement Agreement. In addition to uncertainties of when HCCP operations can begin so power sales can commence, the resolution of unresolved issues with GVEA are also likely to affect the cost of power production. The current mediation is anticipated to address certain operational issues, the results of which would either increase or decrease the cost of producing HCCP power. Effective negotiation of power sales agreements first requires a determination of the cost of power and a realistic estimate of when HCCP operations will commence. More progress in mediation with GVEA is necessary before that can occur.

4. Please provide a copy of AIDEA's ground lease, air permit and coal purchase agreements for HCCP.
5. Please identify interconnect agreements which address spinning reserves and restitution to interior ratepayers for HCCP outages.

AIDEA anticipates that an appropriate ground lease and air permit will be developed in conjunction with the mediation with GVEA.

Under the Project Development Agreement, the negotiation of a coal purchase agreement, interconnect and other agreements will be accomplished through the joint efforts of HEA and AIDEA. For many of the same reasons expressed in the response to question 3, it is difficult to negotiate these agreements without first knowing when AIDEA will obtain from GVEA necessary rights related to the Healy site. For example, in order to obtain a better price, a coal purchase contract may require the purchase of a minimum, annual quantity of coal. It would not be prudent for AIDEA or HEA to commit to purchasing specific annual quantities of coal until after a realistic assessment is made of when HCCP operations will begin, and thus when coal will actually be needed. More progress in the mediation with GVEA is necessary before that can occur.

6. When do you plan to file the Power Sales Agreement with the RCA?

Under the Project Development Agreement between HEA and AIDEA, HEA and AIDEA will jointly determine when to file the Power Sales Agreement with the RCA. Until substantial progress is made with GVEA in the mediation, it would be premature to file the agreement with RCA.

Please provide the following additional information:

1. A copy of the Homer/AEA Project Development Agreement and Power Sales Agreement. If the agreements do not make clear who will bear the conversion and completion, and operating/spinning reserve risks of HCCP, please provide your engineers' assessment of the responsibilities and costs.

Copies are attached. Within the Power Sales Agreement, one paragraph has been redacted. This paragraph addresses certain contingencies related to the litigation/mediation between AIDEA and GVEA, and disclosure could harm HEA's and AIDEA's respective interests.

2. AIDEA built HCCP on GVEA property because AIDEA's engineers determined the plant would be fatally uneconomic if located north of Healy as originally planned. Provide an engineers' assessment of the comparative costs of isolated vs. dual operation of HCCP/ Healy I and the associated cost impact to rate payers of each configuration.

As a preliminary matter, AIDEA does not recall that any AIDEA engineer determined that HCCP economics would be "fatally uneconomic" if located off the

Healy site. However, AIDEA has no plans to operate HCCP at any site other than the Healy site.

The economics of HCCP operations in any configuration will change as the cost of alternative power generation changes. As recently as 2000, the cost of alternative Cook Inlet gas-generated power made HCCP power appear economically unattractive, and in AIDEA's view, significantly contributed to GVEA exercising its contractual rights to terminate the 1991 Power Sales Agreement. However, as Cook Inlet gas resources have diminished, the cost of Cook Inlet gas generated power has increased, and the economics of HCCP generated power have improved. The economics of HCCP generated power as contemplated in current plans looks even better when compared to the cost of other, alternative railbelt power generation.

With respect to the primary question, there is no valid basis to provide an accurate comparison of "isolated vs. dual operation of HCCP/Healy 1" for several reasons.

- a. Some of the economic advantages originally contemplated from the dual operation of Healy #1 and HCCP are no longer available. Since 1999, when HCCP and Healy #1 were both in operation, GVEA has altered its Healy #1 operations to improve its economics and to accommodate neighborhood complaints. While GVEA apparently had good business reasons for making these changes, one consequence has been that the existing coal pile and coal handling facility are no longer reliably adequate for both Healy #1 and HCCP. Because the ability to reliably deliver coal into a coal generating plant is essential, the anticipated economic advantages from dual operation of these facilities has been eliminated.**
- b. An accurate comparison of "isolated vs. dual operation" is contingent upon the results obtained in mediation or litigation with GVEA. Nothing in the existing development plan between HEA and AIDEA precludes the adoption of any mutually beneficial advantages that might accrue to Healy #1 and HCCP. For example, AIDEA contemplates that some facilities will be shared between the two power generating plants, providing economic advantages to both plants. The scope of the beneficial advantages is contingent upon successful resolution of issues with GVEA. AIDEA has limited ability to force GVEA to accept operational criteria that might be beneficial to railbelt ratepayers, but not, in GVEA's view, be beneficial to it.**
- 3. An engineers' assessment of the capital costs to separate HCCP and Healy 1, and the sources of such capital. In the alternative, please provide the joint operating agreement.**

See attached March 28, 2006, "HCCP Condition Assessment and Restart Study" by Shaw, Stone and Webster. The sources of capital, as is described in the agreement between AIDEA and HEA: AIDEA will finance the net capital costs (AIDEA costs

less interim power sales revenues) and HEA will repay that amount over the life of HEA power purchases with interest at 5.25%. *See also* answer to question 2 above.

4. Information on GVEA's 2006 offer to purchase HCCP and to assume all risk for the permitting, conversion, startup and long-term operation of the plant. Provide the engineers' comparative evaluation of the benefits, drawbacks, milestones and risk assessment of the GVEA offer and the Homer/AIDEA agreements.

GVEA did not submit an offer to AIDEA in 2006 to purchase HCCP. GVEA, in the course of mediation, said that it had prepared an offer to purchase HCCP and might submit it to AIDEA, but GVEA first requested AIDEA to confirm that AIDEA would seriously consider the offer. AIDEA gave GVEA written and verbal assurances that AIDEA would seriously consider any offer to purchase HCCP that GVEA submitted. GVEA, however, apparently elected not to submit to AIDEA any offer to purchase HCCP in 2006 because AIDEA did not receive any offer from GVEA to purchase HCCP.

If you have any questions, please call.