

April 22, 2004

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RE: Alaska Intertie – MEA-TLS, Snow-Load, and Repairs

Gentlemen:

The Alaska Energy Authority (AEA) requests a meeting with general managers to discuss replacement of the MEA-TLS section of the intertie, mitigation of snow-load problems, and necessary intertie repairs. While the Intertie Operating Committee (“IOC”) continues to address these issues (most recently at its April 15, 2004 meeting), varied discussions with your organizations, including under the Regulatory Commission of Alaska mandated process regarding the MEA-TLS, leads AEA to conclude that coordination at the general manager level is essential to making efficient progress on these matters. If this meeting serves no other purpose, it should clarify whether anyone disagrees with AEA’s intended course. To assist your preparation for a meeting at the earliest convenient time, following are AEA’s observations and views on these matters:

1. Coordinating construction and repair efforts. The IOC at its April 15, 2004 meeting recommended pursuing Alaska Intertie construction and repair projects including snow-load mitigation/inset towers, SVC control upgrades, and tower foundation repairs. AEA

proposes, to the extent feasible, that project funding, management, engineering, procurement, route selection, environmental, safety, construction, and all other aspects for this work and the MEA-TLS Bypass project be coordinated to capture efficiencies and potential cost savings, and to ensure that the Intertie remains available to the fullest extent possible.

2. Funding Projects. The \$20.3 million legislative appropriation should cover the cost of more than half of the pending projects based on current IOC estimates. AEA, GVEA, ML&P and Chugach previously agreed that additional costs would be covered with debt financing, repayable from future intertie operations. Under the Alaska Intertie Agreement ("Agreement"), such debt financing can be obtained, but each utility has an option under Section 2.2.3 of the Agreement to terminate their participation. AEA will need to follow the notice procedures outlined in that section, and empower utilities to opt out of the Agreement. Therefore, using debt financing to cover additional project costs will require the cooperation of utilities (at least those that choose to remain participants under the Agreement).

AEA interprets the IOC's April 15, 2004, Resolution as supporting debt financing through bonding. The Resolution expresses that IOC expectations were made, in part, "assuming bonding" for the projects. AEA remains committed to assisting in obtaining revenue bonds or other debt financing necessary to complete the various Alaska Intertie projects.

While the debt financing could take several different forms, the least expensive option is likely AEA issued revenue bonds, payable from future intertie operations, with payment guarantees from the utilities – similar to revenue bonds issued for the Bradley Lake Hydroelectric Project. The utility guarantees are likely to improve the bond's ratings, thereby lowering the costs of the debt. Cost savings generated from such bonds would reduce future operating costs by lowering annual debt service payments, and thereby inure to the benefit of utilities using the Alaska Intertie.

3. Appointing ML&P project manager. ML&P, GVEA and Chugach recommended that AEA designate ML&P to be project manager for the MEA-TLS replacement construction project, with the understanding that ML&P will coordinate/ subcontract supporting efforts by GVEA, Chugach and, if applicable, MEA and HEA.

AEA heard a compelling argument that the utilities could undertake and complete the project more efficiently than AEA, and that the utilities are more fully staffed and qualified to complete the projects. Further, it was suggested that further cost efficiencies could be obtained if procurement and project management were merged with ML&P's Eklutna transmission line project.

AEA believes that additional efficiencies could be realized if construction activities related to snow-load mitigation, SVC control upgrades and tower foundation repairs were also merged. AEA therefore proposes that project management for these other projects also be delegated to ML&P.

An additional advantage in designating ML&P project manager arises because it and AEA, as "governmental units" under the Procurement Code, may enter a cooperative agreement under which ML&P will satisfy all procurement requirements for the AEA owned public project.

AEA needs to impose fiscal controls and retain oversight responsibilities as long as the Alaska Intertie remains an AEA owned public asset. The details regarding these matters will need to be coordinated with ML&P and other utilities, and then be incorporated into a project management agreement. This or other agreements will also need to cover our next topic, possible cost overruns.

3. Project completion/cost overruns. Before significant expenditure towards any Alaska Intertie project begins, assurances are necessary that the project will be completed. AEA believes it appropriate for the utilities to assume significant control over the projects, but only after assuming responsibility for ensuring that each project is completed – including ensuring funding for any project cost overruns that might arise.

AEA believes that the funding mechanism discussed in part 2 above would be appropriate if project cost overruns were too great to be covered as part of that year's operating expense. Utilities would cover project cost overruns by pre-authorizing debt financing, repayable over time as part of the intertie's annual operating expenses. While bonding might be inappropriate for such debt financing, securing the rights to borrow and/or having the necessary funds in place would provide an appropriate mechanism to ensure adequate funding to complete the projects.

AEA believes it appropriate to couple utility control and fiscal responsibility for these projects. Decisions made regarding route selection, design, engineering, environmental review, safety, and construction are likely to impact capital as well as operating and maintenance expenses, and will dictate whether the project is completed on budget. Thus, each of those decisions will almost certainly impact future operating costs payable by the utilities using the Alaska Intertie. With those financial incentives, AEA believes the utilities are well positioned to take a lead role determining the best long-term solution to issues that arise during each project's life.

4. Allocating appropriated funds. AEA has heard various utility arguments regarding whether the \$20.3 million appropriation should be used on the MEA-TLS bypass, mitigation of snow-load problems, or other Intertie repairs. The proposed coordinated approach to project management and funding will result in completion of all intertie project needs. If all parties work in a cooperative fashion, we should be able to expedite obtaining funding and starting each project, and thereby eliminate any concern over which project is started first.

However, to the extent it remains an issue to anyone, AEA intends to use the \$20.3 million appropriation to complete the MEA-TLS bypass project before using any of that funding source for any other intertie project needs. AEA's impression from background information associated with the appropriation is that the legislature intended the appropriation to be used first for the MEA-TLS bypass project. AEA intends to honor that legislative intent.

AEA also commits itself to working with the utilities to expedite obtaining debt financing to provide funding for all other project needs. In that regard, AEA views very positively the IOC's April 15, 2004, resolution as it appears to contemplate expeditiously obtaining such necessary funding through revenue bonds.

AEA looks forward to meeting so that we can collectively expedite addressing the needs of the Alaska Intertie. Art Copoulos, AIDEA Project Manager, will be contacting you in the next few days to arrange this meeting. If you have any other matters that you would like to address at

this meeting, please share the topics with the other utility general managers and AEA as soon as possible.

Sincerely

Ron Miller
Executive Director