

April 8, 2003

Mr. James Keselberg, Regional Manager
Western Area Power Administration – Sierra Nevada Region
114 Parkshore Drive
Folsom, California 95630

Dear Jim:

The California ISO is committed to work with Western Area Power Administration – Sierra Nevada Region (Western), as it prepares to implement its Post-2004 Marketing Plan and considers its options for meeting its customers' needs following the expiration its existing transmission service contracts, at the end of 2004. As committed, therefore, the ISO formally presents this offer to prepare an ISO Metered Subsystem (MSS) agreement for Western and the U.S. Bureau of Reclamation (USBR). We believe that the MSS option is viable, and we believe that it presents superior cost and other alternative benefits to any consideration of an independent Federal Control Area.

As you are aware, the ISO is concerned about coordinated operations, grid reliability, and cost implications of any Western decision, for California electricity consumers and ratepayers. Continued provision of ISO Control Area services for Western and its customers avoids the complexity and increased costs inherent in creating multiple Control Area coordinated operations for the California-Oregon Transmission Project (COTP) and the California-Oregon Intertie (COI), for the Pacific AC Intertie (PACI) and Malin-Round Mountain systems, and for Western's systems within northern California. The better option is for Western and USBR to become an MSS within the ISO Control Area.

In developing the MSS alternative, the ISO has resolved many of the issues municipal and other governmental utilities have had with the design of the ISO markets. Evidence of this is seen in the fact that three major governmental power entities have entered into MSS agreements within the last year, since the current MSS model was developed. MSS benefits include the principle of cost allocation based on cost causation, the ability to follow MSS load with MSS resources, treatment of MSS resources on an aggregated basis (i.e., using "System Units"), the ability to fully participate in the ISO ancillary service (A/S) and energy markets, and exemption from non-contingency blackouts-, if the MSS is fully resourced.

When evaluating the options of new Control Area or MSS, it is important to recognize that costs and services associated with Control Area or MSS operations/obligations are separate from Western's issues associated with

transmission service arrangements or transmission capacity allocations. This MSS proposal addresses issues associated with scheduling, settlements, and operation of MSS loads and resources.

Neither the ISO MSS option nor the option of a new Federal Control Area directly resolves transmission service issues for delivering energy to Western customers using the ISO Controlled Grid or capacity allocations on the Pacific AC Intertie, following termination of Western's long standing contract with California companies for Extra High Voltage Transmission and Exchange Service (EHV Contract) at the end of 2004. We recognize that these transmission access issues must be addressed, but we consider them independent of an analysis of the costs and benefits of Western's options of forming an independent Federal Control Area or operating as an MSS within the ISO Control Area.

ISO Staff will be meeting with Western staff within the week to formally present the ISO's offer to negotiate an MSS agreement specifically configured to meet Western's and USBR's requirements. The ISO's objective is to provide Western with a lower cost alternative that meets Western's and USBR's operational needs and retains Western as an integral part of the ISO Control Area.

Thank you for your consideration. I am available to address any questions.

Regards,

Randy Abernathy
Vice President, Market Services

cc: Howard Hirahara, Western
Kyle Hoffman CAISO