Southwest Power Pool put many building blocks in place during 2007 to form a firm foundation to meet the formidable challenges facing our industry, including growing energy demands in a carbon-constrained environment. We achieved three ambitious goals when we launched the Energy Imbalance Service market, were designated as a Regional Entity, and began operating in our new coordination center. In addition, we have set a strong foundation on which to expand the transmission system across our footprint.

SPP’s Energy Imbalance Service market was successfully implemented on February 1, 2007. After a seamless launch and nearly a year of operation, we are pleased to report that it is functioning as planned in facilitating more efficient use of the transmission network, with a high level of market participation and price stability. While prepared for numerous early settlement disputes due to the market’s newness and others’ experiences, we are pleased to report that there have been very few disputes to date. This market serves as an important building block for ancillary services markets that are contemplated in our strategic plan to better manage demand response and energy efficiency, and the variability of many renewable resources.

Another major achievement during the year was SPP receiving approval from the Federal Energy Regulatory Commission to serve as a Regional Entity (RE) supporting the North American Electric Reliability Corporation (NERC). NERC was appointed as the Electric Reliability Organization (ERO) for the United States, with the responsibility for setting and ensuring compliance with mandatory planning and operating standards for the nation’s bulk electric network. As a founding member of NERC, SPP has served as a reliability council since 1968 and is now specifically delegated to perform and oversee some of NERC’s responsibilities for our region.

Implementation of these new responsibilities was now specifically delegated to perform and oversee some of NERC’s responsibilities for our region. Implementation of these new responsibilities was relatively simple from an operational standpoint, but created challenges in establishing a business model substantially different from that of other regions.

SPP is the only FERC-jurisdictional entity serving as both a Regional Transmission Organization (RTO) and a Regional Entity. Some in the industry consider that this structure creates conflicts of interest, but through the collaborative efforts of our membership, we developed and implemented a structure which ensures independence of the Regional Entity function while retaining one of SPP’s core values – Reliability and Economics are Inseparable. We now have three trustees who independently oversee SPP’s Regional Entity delegated functions, while we retain the efficiency and effectiveness of a single organization. Clearly, this is a significant building block as we continue market evolution in the new environment of mandatory compliance.

A third major accomplishment occurred during 2007 as we moved critical real-time operations to our new coordination center, providing SPP with the functionality and critical infrastructure security required in today’s environment. We were very pleased that the move occurred unnoticed by our members and customers. The effect of this third major building block is to ensure our own reliable operations and provide the capabilities necessary to meet the needs and expectations of those we serve.

We continued laying building blocks with 77 additional employees in 2007, ending the year with a staff count of just fewer than 300. While we are pleased to add new staff, we are proud to recognize those who have made significant contributions to SPP and the industry: Mike Thomas for completing 30 years of service, and Jeff Rooker and Eddie Watson for completing 25 years. Additions were made to our IT staff to ensure systems are available and functioning properly, to our engineering staff to perform system and generation impact studies, and to our project management group to better manage the myriad of simultaneous projects facing us in an increasingly tightly-controlled environment. Additionally, we implemented an Engineer-in-Training program and several partnerships with universities to ensure a supply of engineering talent into the future.

Looking forward, as a Regional Transmission Organization, we simply must focus more effort on turning plans for new transmission into reality. We have already approved for construction over $700 million dollars in reliability improvements. Additional building blocks have been assembled, including development of policy and process changes that will allow us to improve our transmission planning; our Regional State Committee has overseen a comprehensive process to engender incentives to build new lines based on the economics of the future; and we have completed an extra high voltage study that envisions a much more robust transmission system for the region, which would bring greater reliability to the grid and support significant development of renewable energy. Now, we must work with our members to expand the transmission network to meet future needs.

Achieving our goals will require tremendous vision and leadership throughout SPP. As an RTO and an RE, we believe our economy and environment deserve no less. We look forward to working together with each and every one of you “to keep the lights on” in 2008.
On February 1, 2007, SPP launched its Energy Imbalance Service (EIS) market and began dispatching wholesale electricity. The wholesale energy market allows for more efficient deployment of generation across the SPP region through the establishment of an offer-based market for energy imbalance service.

SPP is operating the EIS market under a tariff approved by the Federal Energy Regulatory Commission (FERC). The SPP tariff is consistent with the mandate of FERC Order No. 2000, which requires Regional Transmission Organizations (RTOs) to provide real-time energy imbalance service and a market-based mechanism for congestion management.

A cost-benefit analysis performed by CRA International on the impact of an SPP EIS market estimated that the entire Eastern Interconnection would realize $1.2 billion in production cost savings over 10 years, over half of which would flow to the SPP region.

Upon launch of the EIS market, SPP joins the ranks of only a few companies worldwide to offer such services. In addition to operating the EIS market, SPP continues to be responsible for coordinating the wholesale electric transmission system and ensuring fair access to the transmission grid.

Transactions went smoothly during the first year of the EIS market. Average prices were consistent with surrounding markets and had more stability. Dispute activity was modest for the 176,355 transactions settled in 2007. Of the 881 disputes granted, 414 occurred in the first three months of market operations. The average dispute amount was $6,700. Disputes were resolved in an average of 23 days, reduced to a 14-day average after the first three months of market implementation.

The EIS market economically dispatched approximately 70% of SPP's generating capacity. EIS market settlements exceeded $2.7 billion in 2007 and accounted for approximately 8% of SPP's energy transactions.

**Energy Imbalance Service Market Launch**

**Building from the Ground Up: 2007 Operations**

The opening of the new operations facility was a major milestone in SPP's history, and will no doubt be the beginning of a new era for the organization. The first building owned solely by SPP, the new operations center went live on April 9, 2007.

The new facility houses SPP's 24x7x365 operations. Moving these functions to another facility provides more security for the operations and data centers, increasing reliability for our members. "Building from the ground up" was a great accomplishment for SPP that will serve its members for many years to come.

Construction of the new 19,000 square foot facility required 225,000 pounds of rebar, 6 million pounds of concrete, 43 miles of cable, 1.9 miles of fiber, 7.3 miles of electrical wire, 4.7 miles of electrical conduit, 5,250 pipe fittings, 266 light switches, and 7 concrete utility vaults.
**EHV Overlay Study**

In 2007, SPP announced to stakeholders the Extra High Voltage (EHV) Overlay Study: the blueprints for the future of SPP’s transmission grid. This report strategically assesses SPP’s future reliability and capacity needs. To meet those needs, it suggests overlaying the SPP footprint with a 500 and 765 kV transmission system and integrating it with the existing EHV systems of Entergy, the Midwest ISO, and PJM Interconnection.

The benefits of an EHV overlay across SPP’s footprint are threefold:

- Enhanced reliability with a stronger transmission system for the communities within SPP’s footprint.
- Greater access to abundant, renewable energy from existing and potential wind farms in the South Central portion of the United States.
- SPP becomes an even more integral part of an enhanced transmission system extending across the Eastern Interconnection, increasing access to a variety of generation resources.

The EHV Overlay Study team considered the challenges of operating the electric system through the year 2026 and identified an optimized package of projects designed to satisfy the needs of SPP and its members.

The study meets the regional participation planning principle of the Federal Energy Regulatory Commission’s Order 890, requiring transmission providers to coordinate with interconnected systems to share plans and identify enhancements.

Updates to the study will include a full economic assessment of alternatives, including a 345 kV option for comparison purposes, along with forecasts in the upcoming American Wind Energy Association / National Renewable Energy Laboratory Wind Vision report, which are expected to have major impacts on SPP’s long-range transmission needs.

**Joint Coordinated System Planning**

The EHV Overlay Study will do much to meet the long-term needs of SPP’s system, but the scope of such a project stretches beyond SPP’s borders. SPP recognizes the need to work with neighboring entities to plan for and build transmission on a continental scale. In 2007 SPP, in conjunction with the Midwest ISO, PJM Interconnection, the National Renewable Energy Laboratory, and the Tennessee Valley Authority, initiated a Joint Coordinated System Plan (JCSP) to focus on interregional, collaborative transmission expansion plans to address reliability and economic needs. On the JCSP, SPP represents its Regional Transmission Organization footprint as well as the planning interests of Entergy Services and E.ON U.S.

The JCSP is collaborating with the Department of Energy on a major Eastern Wind Integration and Transmission Study, expected to be published in 2009. The study will determine the long-term transmission expansion plans needed to
support a 20% or higher national Renewable Portfolio Standard, and evaluate and quantify the operational impacts, ancillary service requirements, and reliability margin impacts associated with large wind development in remote portions of the United States that have the best wind resources.

**Competitive Renewable Energy Zones**

SPP worked with the Electric Reliability Council of Texas (ERCOT) and stakeholders to identify potential solutions for effectively and efficiently collecting and delivering wind resources from Competitive Renewable Energy Zones (CREZs) in Texas to customers, pursuant to Texas’s Senate Bill 20. Independent studies identified that the four best wind zones in Texas are located in the SPP footprint. SPP proposed a plan to interconnect 1,500 – 4,500 megawatts of new wind development in the Texas Panhandle and provide firm deliveries into ERCOT via new high-voltage direct current facilities. SPP continues to work with ERCOT and the Public Utilities Commission of Texas on expansion plans, which are expected to benefit both regions.

**KETA Study**

In early 2007, the Kansas Electric Transmission Authority (KETA) contracted with SPP to perform a study to determine the “best fit” EHV expansion to serve the needs of Kansas and its neighbors. The study focused on Kansas wind development scenarios that would meet a goal of 10% renewable energy by 2010, growing to 20% in 2020. The study evaluated four 345 kV alternatives, including two EHV ties to Nebraska. The study concluded that a new 345 kV tie to Nebraska was the best project for Kansas and SPP to pursue, and KETA passed a motion to proceed with a line from Spearville, Kansas to Axtell, Nebraska.

**SPP Transmission Expansion Plan 2008-2017**

Developed in 2007 with stakeholder input, the SPP Transmission Expansion Plan (STEP) 2008-2017 identifies regional solutions to regional transmission issues. Similar to the 2006 STEP process, the scope of this annual regional study plan is forward-looking, and includes steady-state and dynamic analysis over an extended 10-year planning horizon. The comprehensive plan analyzes scenarios for summer and winter peak loading, reactive reserve margins, evaluations of transmission operating directives, and economic screening and ranking of projects.

The STEP identified approximately $2.2 billion of transmission network upgrades for the years 2008 through 2017. Projects in the plan include new lines, line rebuilds and upgrades, reactive devices, transformers, substation upgrades, and voltage conversions.

Held twice each year, STEP Regional Planning Summits give SPP stakeholders the opportunity to share their thoughts and opinions about the transmission expansion plan. Issues and solutions are evaluated, and case studies are discussed to give stakeholders an idea of what the grid will look like in the future. SPP also holds four local area planning meetings per year to allow stakeholders to discuss other local issues.

**Regional State Committee and Cost Allocation**

The Regional State Committee (RSC), which is comprised of retail regulatory commissioners in the SPP footprint, provides collective state regulatory agency input on the development and cost allocation of the bulk electric transmission system.

The SPP RSC, with the assistance of its Cost Allocation Working Group, continues to be involved with the ongoing administration of the Base Plan funding policy for reliability-based transmission upgrades. In response to SPP’s strategic plan, the RSC is now focusing on an approach to cost allocation associated with economic upgrades.

The RSC plays an important role in the development of specific transmission plans for SPP’s future, and gives attention to strategic issues such as demand response, a longer-term EHV study, and renewables. The RSC draws upon the input and feedback of SPP’s stakeholders as it reaches decisions on these initiatives.

In 2007, 70 transmission projects totaling $179 million were completed by members, including terminal upgrades, rebuilds, conversions, new lines, line reconductors, capacitor banks, and transformers.
Regional Entity Implementation

As part of the Energy Policy Act of 2005, Congress authorized the Federal Energy Regulatory Commission (FERC) to certify an Electric Reliability Organization (ERO). In 2006, FERC certified the North American Electric Reliability Corporation (NERC) as the nation’s ERO and made it responsible for establishing and enforcing mandatory reliability standards for the bulk power system. This is a shift from voluntary compliance standards in place since NERC’s founding, and a major step in the transition to a strong reliability environment.

The ERO delegates enforcement authority to Regional Entities (REs). To be selected as a Regional Entity, an organization must satisfy the criteria required for the ERO to promote effective and efficient management of the bulk power system.

In April 2007, SPP was selected by FERC as one of eight Regional Entities. The SPP RE now has the authority to audit, investigate, and otherwise ensure that NERC Registered Entities (owners, operators, and users of the bulk power system) comply with mandatory reliability standards. The SPP RE is responsible for establishing regional standards for the SPP footprint. Currently, 127 Registered Entities are reporting to the SPP RE. Of those, approximately 80 are non-SPP members located within the SPP footprint.

SPP is the only organization that serves as both a Regional Entity and a Regional Transmission Organization. SPP’s reliability coordination efforts are kept separate from its RE efforts. To ensure that SPP complies with mandatory reliability standards, the organization has created an Internal Standards Compliance department, responsible for coordinating and facilitating the development of compliance plans, policies, procedures, and implementing systems and software to track and monitor compliance programs.

SPP's Regional Entity Trustees (from left): Gerry Burrows, Chair John Meyer, and David Christiano

SUPPLY AND DEMAND

Each year, SPP submits a 411 Form to the Energy Information Administration (EIA), which collects data on actual and projected energy and peak demand, existing and future generating capacity, historical data, and projection of capacity. SPP uses this data in planning models and to monitor trends in load growth and consumption. The EIA uses 411 data from SPP and other organizations to compile national energy forecasts.

Regional Entity Trustees (from left): Gerry Burrows, Chair John Meyer, and David Christiano

BUILDING WITH INTEGRITY: Growing as a Regional Organization

an Internal Standards Compliance department, responsible for coordinating and facilitating the development of compliance plans, policies, procedures, and implementing systems and software to track and monitor compliance programs.

SPP’s Regional Entity Trustees (from left): Gerry Burrows, Chair John Meyer, and David Christiano
**Expanded Training Opportunities**

In March 2007, SPP conducted the first of two Regional BlackStart drills and two Subregional BlackStart drills. These drills, simulating a blackout in all or part of the SPP footprint, provided an opportunity for SPP member companies to practice coordination, communication, and restoration.

One of the main goals of the drills is to offer the training frequently enough for members to become more familiar with their systems and allow SPP operators more hands-on experience with the BlackStart plans of each entity in the SPP footprint. SPP has set a new standard for conducting these drills using simulators. This allows for more participation from multiple locations, as would be the case in an actual emergency situation.

In addition to the BlackStart drills, the SPP Training department held numerous classes and conferences to ensure SPP’s and members’ operators were properly certified according to NERC standards. In 2007, the SPP Training department awarded a total of 13,043 continuing education hours to 338 attendees representing 24 different entities, including SPP.

**New SPP Members**

SPP added three new members in 2007: Mid-Kansas Electric Company, Trans-Elect Development Company, and Kansas Municipal Energy Agency. SPP now has 49 members, including cooperatives, independent power producers, independent transmission companies, investor-owned utilities, marketers, municipals, and state agencies.

**SPP Membership**

<table>
<thead>
<tr>
<th>Role</th>
<th>Number of Members</th>
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<tbody>
<tr>
<td>Investor-Owned</td>
<td>12</td>
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<tr>
<td>Marketers</td>
<td>11</td>
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<tr>
<td>Cooperatives</td>
<td>11</td>
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<tr>
<td>Municipalities</td>
<td>8</td>
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<tr>
<td>Independent Power Producers</td>
<td>3</td>
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<tr>
<td>Independent Transmission Companies</td>
<td>2</td>
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<tr>
<td>State Agencies</td>
<td>2</td>
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</tbody>
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**Cooperatives**

- Arkansas Electric Cooperative Corporation *
- East Texas Electric Cooperative, Inc. *
- Golden Spread Electric Cooperative *
- Kansas Electric Power Cooperative Mid-Kansas Electric Company *
- Midwest Energy, Inc. *
- Northeast TX Electric Cooperative *
- Rayburn Country Electric Cooperative *
- Sunflower Electric Power Corporation * #
- Tex - La Cooperative of Texas, Inc. *
- Western Farmers Electric Cooperative *

**Independent Power Producers**

- Calpine Energy Services, L.P. *
- Redbud Energy *
- Tenaska Power Services *

**Independent Transmission Companies**

- Trans-Elect Development Company, LLC

**Marketers**

- Aquila Power - Aquila, Inc. *
- Cargill Power Markets, LLC *
- Constellation Energy Commodities Group, Inc. *
- Coral Power, LLC
- Duke Energy Americas, LLC *
- Dynegy Power Marketing, Inc. *
- Edison Mission Marketing & Trading, Inc. *
- El Paso Merchant Energy, L.P. *
- Luminant Energy Company, LLC
- NRG Power Marketing, Inc. *
- Williams Power Company, Inc. *

**Municipals**

- Board of Public Utilities (Kansas City, Kansas) *
- City of Clarksdale, Mississippi *
- City of Lafayette, Louisiana *
- City Utilities of Springfield, Missouri *
- Kansas Municipal Energy Agency *
- Oklahoma Municipal Power Authority
- Public Service Commission of Yazoo City, Mississippi *

**State Agencies**

- Grand River Dam Authority *
- Louisiana Energy & Power Authority *

**SPP Contract Participant**

- Southwestern Power Administration #

* Transmission Dependent Member
# Balancing Authority/Control Area within SPP
^ Transmission Owner
BUILDING FOR EXCELLENCE: Staffing

SPP’s projects could not be successfully completed without its knowledgeable staff. Seventy-seven employees were hired in 2007, bringing the total employee count to almost 300.

SECOND ANNUAL LEADERSHIP CONFERENCE

With a growing staff, more effort has been made to cultivate SPP’s knowledge base. In May, the second annual Leadership Conference had over 200 participants from SPP and other Central Arkansas businesses and nonprofit organizations. Discussions were led by Dr. David Garvin of Harvard Business School. Divided into groups, attendees participated in discussions of three case studies and were asked to share their thoughts on how the scenarios applied to SPP’s challenges and issues. The successful event allowed all employees to share a common learning experience.

LEADERSHIP TRAINING

Another valuable learning experience for employees was an eight-week Leadership Training class. Participants included all new supervisory staff and employees identified by their supervisors as having leadership potential. Topics included recognizing achievements and human potential, leading effective meetings, the delegation process, managing conflict and change, developing flexibility, and celebrating success. Classroom sessions included table discussions, group discussions, role-playing, homework, and weekly presentations.

ENGINEER-IN-TRAINING PROGRAM

One of SPP’s value propositions is Relationship-Based. One way SPP is cultivating long-term relationships is through the Engineer-in-Training program, which was implemented in July. The 18-month program is designed to attract and hire highly qualified Bachelor of Science in Electrical Engineering graduates and cross-train them in key functional areas such as operations, engineering, market development, and compliance. The Engineer-in-Training Program allows SPP to assess candidates’ preferences and place them into full-time roles based upon their abilities.

BUSINESS MODEL COMPLETED

In November, the new SPP Business Model was introduced to employees as a visual representation of SPP’s overall strategy and organization. The business model is comprised of SPP’s critical functions; leadership style; culture; people; strategy; and organizational structures, controls, and processes.

BUILDING WITH EXPERIENCE: Industry Outreach

THE ISO/RTO COUNCIL

In 2007, SPP continued its participation with the ISO/RTO Council (IRC), an industry organization comprised of ten Independent System Operators and Regional Transmission Organizations in North America. SPP built a website for the organization, iso-rto.org, which was successfully launched in June.

SPP participated in an IRC media briefing and Congressional forum in Washington, D.C. in October. President Nick Brown spoke to reporters and Congressional staffers about the need for more transmission to move renewable energy, such as wind and hydro, to populated areas. He stressed the importance of having a national approach to the development of renewable energy generation and transmission. Attendees of the two events received three new reports written by the IRC (available on iso-rto.org):

• Increasing Renewable Resources: How ISOs and RTOs are Helping Meet this Public Policy Objective
• Progress of Organized Wholesale Electricity Markets in North America
• Harnessing the Power of Demand
**Participation in Industry Organizations**

SPP executives participated in a number of other industry organizations in 2007, including the Southeastern Association of Regulatory Utility Commissioners, National Association of Regulatory Utility Commissioners, Edison Electric Institute, Federal Energy Regulatory Commission Technical Conferences, and the Electric Power Research Institute, for which President and CEO Nick Brown serves as a board member.

Brown was appointed to the Arkansas Governor’s Commission on Global Warming, which was established to study issues related to global warming and the emerging carbon market. Created during the 2007 legislative session, the commission’s goal is to attract clean and renewable energy industries and to reduce consumer dependence on current carbon generating technologies. The commission will work to establish a pollutant reduction goal and a comprehensive strategic plan.

**Central Africa Power Pool Visits SPP**

In 2007, SPP reached out to other industry organizations in an effort to expand the knowledge of those entities. Members of the Central Africa Power Pool visited SPP to gain insight into the formation of a power pool. Employees of several Japanese utilities also visited SPP to learn about transmission planning.

**Other Initiatives**

To promote knowledge sharing, SPP donated $10,000 to the University of Arkansas Information Technology Research Center Member Fund. The Information Technology Research Institute is an interdisciplinary unit within the Sam M. Walton College of Business, whose mission is to advance the development and use of information technology for enhancing the performance of individuals and organizations.

SPP hosted the Energy Intermarket Surveillance Group (EISG) Market Conference in Little Rock in April. The EISG provides a forum for the private exchange of ideas concerning issues, techniques, and procedures among those responsible for the surveillance of the competitiveness of wholesale electricity markets. Electricity markets from across the nation were represented, as well as those in Canada, New Zealand, France, the Netherlands, and the Philippines.

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The active participation of our membership is vital to ensuring that benefits outweigh costs in the implementation of services. SPP's administrative fee, the primary source of cost recovery, was 19¢/MWh in 2007 as compared to 16¢/MWh in prior years. 2007 was the first full year SPP provided independent tariff services to two non-member utilities, allowing us to further maximize our embedded infrastructure. Provision of these services allowed SPP to limit the increase in the administrative fee. The increase in 2007 reflected the growth of the company and the services provided, and will support SPP's operations in 2008.

Our conservative financial profile resulted in Fitch Ratings issuing SPP a debt and issuer rating of “A”. This rating is vitally important for SPP as it enhances opportunities to obtain low-cost capital to fund future initiatives. During 2007, SPP obtained $30 million in term financing at an attractive credit spread, and reached agreement with a lender to obtain a $20 million revolving credit facility.

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SPP continues to be the low-cost provider of regional services, in large part a result of robust member participation in SPP's development.

- Tom Dunn, Chief Financial Officer