STATE OF MAINE
PUBLIC UTILITIES COMMISSION

Docket No. 2001-434

April 30, 2002

BANGOR HYDRO-ELECTRIC COMPANY
Approval of Special Rate Agreement with
Lincoln Pulp & Paper Company, Inc.

ORDER

WELCH, Chairman; NUGENT and DIAMOND, Commissioners

SUMMARY

We approve an amendment to the Special Rate Agreement (the 2001 Agreement) between Bangor Hydro-Electric Company (BHE) and Lincoln Pulp & Paper Co., Inc. (Lincoln). We also approve a stipulation among BHE, Lincoln and the Office of the Public Advocate (OPA) that includes, among other things, the recommended ratemaking treatment associated with the Special Rate Agreement.

BACKGROUND

In June, 2001, Lincoln and BHE entered into the 2001 Agreement to resolve issues raised by unbundling generation service from transmission and distribution service in Lincoln's prior special rate contract called the Power Sales Agreement (PSA).[1] The unbundling effort was made more complicated because Lincoln had filed for protection under Chapter 11 of the U.S. Bankruptcy Code in September 2000. Lincoln had been unable to secure a generation service contract with a competitive electricity provider (CEP) at a price below BHE's then-current standard offer price, even though all parties agreed that customers exhibiting Lincoln's load characteristics should generally be able to obtain lower-priced generation service from a CEP than through the standard offer provider. Because the PSA-bundled electricity price was lower than the then-current standard offer price, and therefore unbundling might result in payments from BHE to Lincoln, the Commission directed the parties to explore service from a CEP, even if such service might require BHE to provide credit guarantees.

As a result, BHE, Lincoln and the OPA, with the assistance of our Advisory Staff, negotiated the 2001 Agreement to replace the PSA. The term of the 2001 Agreement is from July 1, 2001 through March 31, 2006. During the initial period, defined to be July 1, 2002 through March 31, 2002, Lincoln received the benefit of the PSA, which meant that Lincoln received delivered energy and capacity for 6¢/kWh. As the special contract unbundling statutory provision (35-A M.R.S.A. §3204(10)) imposed the power supply cost risk on BHE, Lincoln agreed that BHE would arrange for a CEP to supply power in

[1] The Electric Restructuring Act, 35-A M.R.S.A. § 3201-3217, prohibits BHE from providing generation services, and therefore requires BHE to unbundle pre-restructuring special rate contracts such as the PSA.

the manner chosen by BHE to minimize power supply costs and BHE agreed to provide a credit guarantee and a take-or-pay commitment to the CEP. Under this arrangement, Lincoln's power supply costs in the initial period were significantly less than 6¢/kWh. Because the unbundling for most of the initial period was subject to reconciliation by the stipulation in BHE's initial T&D rate case (Docket No. 97-596), T&D ratepayers directly benefited when the increased contribution by Lincoln was recognized in rates when stranded costs were reset in Docket No. 2001-239, effective on March 1, 2002.

The second period of the 2001 Agreement runs from April 1, 2002 through March 31, 2006. Lincoln's T&D price during the second period is based upon a profit-based index. The index has a minimum price of BHE's FERC-approved Open Access Transmission Tariff (OATT). The index uses a proxy for Lincoln's profits, and as the proxy's profitability goes up, the index produces higher T&D prices. During the second period, Lincoln will also pay BHE an additional amount if Lincoln's combined generation cost and T&D cost is less than 6.2¢/kWh. Lincoln pays BHE 60% of the difference between 6.2¢/kWh and the "rebundled" electricity price. In addition, during this second period, Lincoln has the option of seeking one-year full requirements generation service contracts for which BHE will provide an unconditional credit guaranty and a take-or-pay commitment. In any year that Lincoln invokes BHE's credit guaranty, Lincoln must exercise due diligence to obtain the lowest price contract.[2]

In orders dated June 27, 2001 and July 17, 2001, the Commission approved the 2001 Agreement. The Commission reasoned that the 2001 Agreement assured that the contribution to stranded costs received from Lincoln during the initial period would be maximized. Without BHE's power supply arrangement and its credit guarantee to the CEP, Lincoln would have remained on standard offer service through the initial period. The value provided by the generation savings (approximately $1.5 million) outweighed, in the Commission's assessment, the risk that Lincoln would cease operation in the initial period and thus require BHE to fulfill its take-or-pay commitment. Moreover, the credit risk was minimized by a provision in the 2001 Agreement that requires Lincoln to pay its power supply and T&D bill every two weeks by Electronic Funds Transfer (EFT).

The Commission also found significant benefits during the second period of the 2001 Agreement. Lincoln is BHE's second largest customer, and provides a significant contribution to BHE's T&D costs. The Commission also found merit in the concept of a minimum contribution, with the opportunity of increased contribution based upon an objectively-determined profit index. The Commission also concluded that the addition of more contribution if the "rebundled" price of electricity to Lincoln falls below 6.2¢/kWh confers benefits to BHE and ratepayers.

These benefits in the second period of the 2001 Agreement had to be weighed against the risks arising from the credit guarantee and the take-or-pay requirement.

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[2] If BHE believes that Lincoln did not exercise due diligence, BHE may petition the Commission to resolve the matter. Both parties agree to be bound by the Commission's determination.

The Commission found those risks, however, to be significantly mitigated by the two-week EFT obligations and the fact that any power supply contract will be for no more than 12 months. Moreover, the greater availability of a competitive power supply arrangement could be important to further Lincoln's ability to successfully reorganize. On balance, then, the Commission concluded that the 2001 Agreement served the public interest and approved it.

Lincoln's initial period contract with its CEP expired on March 31, 2002. During March 2002, Lincoln solicited bids from CEPs for generation service of one, two and three year terms, beginning April 1, 2002. BHE agrees that Lincoln conducted a reasonable bid process. Lincoln and BHE agree that all bids for service in year 1, or April 1, 2002 through March 31, 2003, were clearly less attractive than the standard offer for large non-residential customers.

As part of the bid solicitation process in March, Lincoln also received bids for the period described as year 2 and year 3, or April 1, 2003 through March 31, 2004 and April 1, 2004 through March 31, 2005. Because of the attractiveness of one of the bids for years 2 and 3, Lincoln, after consulting with BHE, OPA and Commission Staff, decided to pursue a two-year supply contract with service beginning on April 1, 2003.

After lengthy discussions, Lincoln and the bidder, Sprague Energy Corp. (Sprague) have entered into a retail electricity purchase and sale agreement (Sprague contract). The term of the Sprague contract is from April 1, 2003 through March 31, 2005. Sprague agrees to provide firm all requirements electricity service to Lincoln during the term.[3] The Sprague contract, and its bid, are contingent on BHE providing a credit guarantee in case of nonpayment by Lincoln and a take-or-pay commitment of the power supply in case Lincoln defaults under the contract or ceases operation. Sprague and BHE have entered into a "Guaranty Agreement" that satisfies Sprague's contingency. Because the 2001 Agreement permits BHE to accept a take-or-pay commitment of a power supply contract for a duration of no more than 12 months, Lincoln and BHE have executed a First Amendment to Special Rate Agreement. The First Amendment authorizes and requires BHE to provide the take-or-pay provision as described in the Guaranty Agreement for the 2-year term. The First Amendment also describes the bankruptcy treatment that must be accorded any claim that BHE obtains because it is called upon to provide money to Sprague pursuant to the Guaranty Agreement.

As the First Amendment amends a special rate contract approved by the Commission pursuant to 35-A M.R.S.A. § 703(3), the amendment also must be approved by the Commission to become effective. The parties to this docket, Lincoln, BHE and the OPA, have filed a stipulation recommending Commission approval of the First Amendment. The stipulation also recommends the ratemaking treatment that should be accorded the 2001 Agreement and First Amendment, and accounting orders that should be issued to accomplish the future rate treatment.

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[3] The Sprague contract is confidential as proprietary business information.

DECISION

All parties to this matter have joined the Stipulation. For this reason, and for the reasons explained in our July 17, 2001 Order, the first two criteria we apply when reviewing a stipulation, whether the parties joining the stipulation represent a sufficiently broad spectrum of interests and whether the process was fair to all parties, are satisfied. Thus, we are left to decide whether the stipulated result is reasonable and not contrary to legislative mandate, as well as in the public interest. *See Central Maine power Company, Proposed Increase in Rates*, Docket No. 92-345(II), Detailed Opinion and Subsidiary Findings (Jan. 10, 1995) and *Northern Utilities, Inc., Proposed Environmental Response Cost Recovery*, Docket No. 96-678, Order Approving Stipulation (April 28, 1997).

We find that the First Amendment is a reasonable extension of the special rate arrangement already approved in the 2001 Agreement. Last year, when we authorized BHE to extend a credit guaranty and up to a 12-month take-or-pay commitment to Lincoln, we reasoned that maintaining a revenue contribution from Lincoln beyond March 31, 2001 is important to BHE and its customers. With the closure of the Holtrachem facility, Lincoln became BHE's second largest customer. As a large customer, Lincoln has a significant impact on the level of BHE's core rates. It is, therefore, important to BHE and its ratepayers to promote the viability of Lincoln to maximize its contribution toward BHE's fixed costs. July 17, 2001 Order, at 4. Electricity is a significant cost to Lincoln's business. As an entity currently under the protection of Chapter 11 of the Bankruptcy Code, a reasonably-priced contract for electricity, for two and three years from today, likely is not available to Lincoln without the First Amendment. We believe that providing Lincoln with three years of stable electricity prices, which is accomplished by the present standard offer and the 2-year supply agreement with Sprague, will significantly improve the long-term viability of Lincoln and therefore maximize Lincoln's contributions toward BHE's fixed costs.

Although the prices in the Sprague Contract are confidential and therefore not mentioned in our order, we can note that the Sprague prices are reasonable and generally consistent with existing market conditions. We also believe the decision to contract for power supply at current market prices for an additional 2-year term is reasonable and prudent. Therefore, we conclude that Lincoln has exercised due diligence to obtain the lowest price supply contract by entering the Sprague Contract.

Our review is not complete, however, because Lincoln's contract requires BHE to extend greater value to Lincoln than we authorized in approving the 2001 Agreement, namely a 24-month take-or-pay commitment, a commitment that, although made today, does not begin until almost a year from now. The First Amendment, therefore requires BHE to accept electricity market price risk up to 36 months from now.

In the context of this case, we find that the extended take-or-pay commitment is reasonable. While BHE and its ratepayers do face increased risks, those risks are

manageable. The downside to ratepayers occurs if market prices fall or, if market prices rise but only slightly, BHE may not be able to cover the retail-wholesale spread if the contract needs to be liquidated. However, based on recent market history, the likely range of losses resulting from a drop in market prices appears somewhat less than the likely range of benefits possible if market prices increase. In other words, the potential magnitude of the upside appears somewhat higher than the downside. Further, BHE has locked in its right to these potential benefits, by assuring in the First Amendment that any market price upside will belong to BHE and its ratepayers rather than the bankrupt's estate. In addition, to the extent that the take-or-pay provision does result in a loss to BHE, its claim against Lincoln will receive second priority administrative claim status, which improves the chances BHE will recover at least some of its loss.

As described, under the assumption that Lincoln closes or defaults and BHE assumes the take-or-pay requirement, the risks presented by the increased take-or-pay exposure appear less than the potential benefits to BHE and ratepayers by the First Amendment. Of course, as we already mentioned, the longer-term, stable, reasonably-priced electricity is expected to enhance Lincoln's viability and therefore increase the likelihood that BHE will not be required to assume the take-or-pay commitment. Moreover, assuming Lincoln does continue to operate, because the Sprague contract assures a "rebundled" electricity price of less than 6.2¢/kWh, BHE and ratepayers are able to lock in some additional stranded cost contribution from Lincoln and avoid the risk that future "re-bundled" prices will be higher than today's, or even higher than 6.2¢/kWh.

We also find that the proposed ratemaking and accounting orders called for in the Stipulation are reasonable. Indeed, we believe the proposed ratemaking treatment is consistent with the expectations of the Commission and the parties' in our July 17 Order. In the recently completed stranded cost revenue requirement docket (Docket No. 2001-239), non-core revenue from Lincoln was estimated at nearly the floor amount. This was a reasonable assumption based on circumstances at the time the calculations were performed. It now appears, however, that the profitability index and the "re-bundled" shared-savings adjustment, will likely provide significantly greater contribution, at least through February 28, 2003. Conversely, the credit guaranty and take-or-pay commitment could result in considerably lower net contribution or even a loss in the period April 1, 2003-March 31, 2005. Therefore, we agree with the stipulating parties that it is fair for ratepayers to both receive the benefits and bear the burdens of Lincoln's special rate arrangement, including the risk that Lincoln may shut down altogether. We also agree with the stipulating parties that our accounting orders and future ratemaking treatment should reconcile only the PUC-jurisdiction revenues, (distribution and stranded cost revenues), and not transmission revenues.

Lastly, the stipulating parties also seek to adjust stranded cost rates for the period June 1, 2002 through May 31, 2003 to recognize a portion of the additional Lincoln contribution from the "re-bundled" price shared-savings during the current standard offer period in order to offset an anticipated transmission rate increase this summer. This recommendation is reasonable. Rate stability is always important. Although the different rate designs for stranded cost and transmission rates means the

two rate changes will not be perfectly offset, the impact of a transmission rate increase will be lessened if accompanied by a stranded cost rate decrease.

In addition, as the Guaranty Agreement between BHE and Sprague requires BHE to provide a credit guarantee for longer than 12 months, BHE seeks Commission approval of the Guaranty Agreement pursuant to 35-A M.R.S.A. § 902. As the guaranty represents a potential indebtedness of BHE that is payable for a period of more than 12 months after the Guaranty Agreement is entered into by BHE, the Guaranty Agreement constitutes "other evidences of indebtedness" within 35-A M.R.S.A. § 901, which in turn requires Commission authorization for BHE to "issue" the guaranty by 35-A M.R.S.A. § 902. For the reasons stated above, we grant that authorization.

Accordingly, we

O R D E R

1. That the attached Stipulation filed in this docket on April 30, 2002, is approved and incorporated herein;

2. That the First Amendment to Special Rate Agreement, attached to the April 30 Stipulation, is approved pursuant to 35-A M.R.S.A. § 703;

3. That the Guaranty Agreement between Bangor Hydro-Electric Company and Sprague Energy Corp., filed April 30, 2002, is approved pursuant to 35-A M.R.S.A. § 902;

4. That Bangor Hydro-Electric Company shall account for its transactions involving the Special Rate Agreement, as amended, and all the related contracts and agreements, in a manner consistent with this Order and Stipulation approved by this Order.

Dated at Augusta, Maine, this 30th day of April, 2002.

BY ORDER OF THE COMMISSION

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Dennis L. Keschl
Administrative Director

COMMISSIONERS VOTING FOR: Welch
Diamond

COMMISSIONER ABSENT: Nugent

STATE OF MAINE

PUBLIC UTILITIES COMMISSION

BANGOR HYDRO-ELECTRIC COMPANY **STIPULATION**
Re: Approval of Special Rate Agreement
With Lincoln Pulp & Paper Co., Inc.

Docket No. 2001-434

Bangor Hydro-Electric Company (BHE), Lincoln Pulp & Paper Co., Inc. (Lincoln) and the Office of Public Advocate hereby agree and stipulate as follows.

PURPOSE

1. The purpose of this Stipulation is to settle all issues in this proceeding, to avoid a hearing on those issues, and to expedite the Public Utilities Commission's consideration and resolution of the proceeding. The provisions agreed to herein have been reached as a result of discussions among the Parties in this case.

PROCEDURAL BACKGROUND

2. BHE and Lincoln were parties to a Power Sales Agreement dated December 31, 1996 which was unbundled in accordance with 35-A M.R.S.A. § 3204 (10) and the unbundling was approved by this Commission on June 16, 2000 under Dkt. No. 2000-180.

3. On September 22, 2000, Lincoln filed in the United States Bankruptcy Court for the District of Maine (the "Bankruptcy Court") seeking protection under Chapter 11 of the United States Bankruptcy Code, Dkt. No. 00-11614.

4. On June 27, 2001 BHE and Lincoln executed a Special Rate Agreement (the "2001 Agreement") which in part (i) rescinds and terminates the 1996 Power Sales

Agreement; (ii) provides a discounted T&D rate for Lincoln through March 31, 2006; and (iii) allows Lincoln to elect to require BHE to provide a credit guaranty and take or pay provision for four successive one year generation contracts with a CEP from April 1, 2002 through March 31, 2006. The 2001 Agreement was approved by this Commission on June 27, 2001 under Dkt. No. 2001-434 (Part II Order dated July 17, 2001) and approved by the Bankruptcy Court on June 28, 2001 under Dkt. Entry 211 in Case No. 00-11613.

5. On April 30, 2002 Lincoln and Sprague Energy Corp. (Sprague) entered into a Retail Electric Sale Confirmation Agreement (the "Supply Agreement") attached hereto as Exhibit A (Designated Confidential Information) whereby Sprague has agreed to provide generation service to Lincoln from April 1, 2003 through March 31, 2005. The Supply Agreement is subject to BHE executing the Guaranty Agreement attached hereto as Exhibit B (the "Guaranty Agreement"), approval of this Stipulation, and approval of the Supply Agreement by the Bankruptcy Court.

6. On April 30, 2002 BHE and Lincoln entered into the First Amendment to the 2001 Agreement (the "First Amendment"). The First Amendment is attached hereto as Exhibit C. The First Amendment provides for BHE entering into the Guaranty Agreement. The First Amendment is subject to approval by this Commission and the Bankruptcy Court.

APPROVALS AND FINDINGS

The parties to this Stipulation agree and recommend that the Commission conclude this proceeding by issuing a Supplemental Order which approves, accepts and adopts this Stipulation including the following provisions:

1. Amend the Commission's Order dated June 27, 2001 to authorize BHE to enter into the First Amendment attached hereto as Exhibit C.

2. Effective as of March 1, 2002, BHE will defer for future recognition in stranded cost rates:

   a) any Net Stranded Cost Revenues received from Lincoln; plus

   b) any Net Benefit (if positive) or Net Cost (if negative) to BHE associated with its entry into and related to the 2001 Agreement, as amended.

The Net Stranded Cost Revenues shall be calculated as the difference between the actual non-transmission revenues received from Lincoln associated with BHE's entry into and related to the 2001 Agreement, as amended, and the estimated stranded cost revenue contribution from Lincoln used to set stranded cost rates in Docket No. 2001-239.

The Net Benefit or Net Cost will be calculated as the difference between the revenue or value received by BHE, and the expenses incurred by BHE, associated with its entry into and related to the 2001 Agreement, as amended.

The amount of the deferral may be positive or negative and will include carrying costs computed using the Company's weighted average cost of capital, including the return on common equity of 11% as approved in Docket No. 2001-239.

Finally, any deferrals permitted under this Paragraph shall be offset by the stranded cost revenue reductions implemented under Paragraph 3.

3. In anticipation of the receipt by BHE of additional stranded cost revenues above those assumed in Docket No. 2001-239, BHE is authorized, subject to final Commission approval, to reduce stranded cost rates to core customers from the period June 1, 2002 through May 30, 2003 in order to provide an offset to the anticipated increase in FERC transmission rates scheduled to go into effect on June 1, 2002. The total reduction in stranded cost revenue will be intended to equal, but not exceed, the anticipated total increase in FERC transmission revenues related to core customers over the period June 1, 2002 through May 30, 2003; provided, however, that such reduction may not exceed the anticipated Net Stranded Cost Revenues expected to be collected from Lincoln over the period March 1, 2002 through February 28, 2003. The total reduction in stranded cost revenue will be allocated to core classes only and will be allocated as an equal percentage reduction using the core stranded cost rates, revenues and billing units reflected in BHE's compliance filing approved by the Commission in Docket No. 2001-239. Such reduction may be implemented notwithstanding any limitations provided in Docket No. 2001-239.

4. Nothing in paragraph 2 nor an Order approving this Stipulation shall constitute a pre-determination as to the prudence of a) BHE's decision on whether to take title to or control of electric power or instead to invoke the Termination Payment under the take or pay provisions of the Guarantee Agreement, if applicable, or; b) BHE's actions in disposing of any electric power it may take title to or control of in connection with the take or pay provisions of the Guaranty Agreement.

5. BHE is authorized, pursuant to 35-A M.R.S.A. §901, to enter into the Guaranty Agreement.

PROCEDURAL STIPULATIONS

1. The parties to this Stipulation hereby waive their rights to request reconsideration pursuant to Section 1004 of the Commission's Rules of Practice and Procedure (65-407 C.M.R. 110), to appeal pursuant to 35-A M.R.S.A. § 1320, or to otherwise seek reconsideration or judicial review of any Commission Order approving this Stipulation.

2. The parties to the Stipulation hereby waive any rights that they have under 5 M.R.S.A. §9062(4) and Section 742 of the Commission Rules of Practice and Procedure to the extent necessary to permit the Advisory Staff to discuss this Stipulation and the resolution of this case with the Commissioners at the Commission's schedule deliberations, without providing to the parties an Examiners Report or the opportunity file Exceptions.

3. The record on which the parties enter into this Stipulation and on which the Commission may base its determination whether to accept and approve this Stipulation shall consist of BHE's request for approval and all attachments thereto and any other material furnished by the Advisory Staff to the Commission, either orally or in writing, to assist the Commission in deciding whether to accept and approve this Stipulation.

4. This Stipulation shall not be considered legal precedent, nor shall it preclude a party from raising any issues in any future proceeding or investigation on similar matters subsequent to this proceeding.

5. This Stipulation represents the full agreement between the parties to the Stipulation and rejection of any part of this Stipulation constitutes a rejection of the whole.

6. If not accepted by the Commission in accordance with the provisions hereof, this Stipulation shall not prejudice the positions taken by any party before the Commission in this proceeding and shall not be admissible evidence therein or in any other proceeding before the Commission.

Respectfully submitted this 30th day of April, 2002.

OFFICE OF THE PUBLIC ADVOCATE

_____

By:
Its:

LINCOLN PULP & PAPER CO., INC.

_____

By:
Its:

BANGOR HYDRO-ELECTRIC COMPANY

_____

By:
Its:

FIRST AMENDMENT
to
SPECIAL RATE AGREEMENT
between
Bangor Hydro-Electric Company and Lincoln Pulp & Paper Co., Inc.

This is the First Amendment to the Special Rate Agreement dated June 27, 2001 (the "First Amendment") made April 30, 2002 between LINCOLN PULP & PAPER CO., INC., a corporation incorporated under the laws of the State of Delaware, having its principal office at the Town of Amherst, Commonwealth of Massachusetts, and having a place of business at Lincoln, Maine (hereinafter referred to as "Lincoln") and BANGOR HYDRO-ELECTRIC COMPANY, a public utility incorporated under the laws of the State of Maine, having a principal office at 33 State Street, City of Bangor, State of Maine (hereinafter referred to as "BHE"). BHE and Lincoln may be collectively referred to as the "Parties."

WHEREAS, pursuant to the terms of the 2001 Special Rate Agreement, BHE currently provides Lincoln with transmission and distribution service ("Delivery Service") to Lincoln's facility located within BHE's service territory at 50 Katahdin Avenue, Lincoln ME 04457 (the "Facility").

WHEREAS, pursuant to the terms of the 2001 Special Rate Agreement Lincoln has solicited bids for licensed Competitive Electricity Provider to provide future generation service to Lincoln,

WHEREAS the winning bid by Sprague Energy Corp. ("Sprague Energy") is a two-year bid and is conditioned upon BHE providing a two-year credit guaranty and take or pay provision.

WHEREAS, BHE's credit guaranty and take or pay provision attached hereto as Attachment A (the "Guaranty Agreement") will induce Lincoln to remain a BHE customer, thus providing a contribution to BHE's fixed costs to the benefit of BHE's other customers;

NOW, THEREFORE, in consideration of the mutual promises contained herein, the sufficiency of which is hereby acknowledged, the Parties hereby agree as follows:

1. Section 7 (a) of the Special Rate Agreement is hereby amended to provide that BHE shall provide an unconditional credit guaranty and take or pay provision for a two year Generation Service Agreement from April 1, 2003 to March 31, 2005 between Sprague Energy and Lincoln (the "Supply Agreement").

2. Subject to approval of the United States Bankruptcy Court for the District of Maine in Lincoln's currently pending Chapter 11 proceedings and except as set forth below in this paragraph, BHE shall have an allowed, superpriority, administrative claim pursuant to 11 U.S.C. §503(b) and §364(c)(1) in the amount of any loss or damage incurred by BHE as a result of the performance of its obligations under the Guaranty Agreement and this First Amendment, including without limitation any amounts paid by BHE under the Guaranty Agreement (the "BHE Administrative Claims"), (provided, however, that in no event shall the BHE Administrative Claims be paid from, or in any respect attach to Avoidance Actions, as defined herein) and such BHE Administrative Claims shall have priority over any and all other administrative claims in the Chapter 11 proceedings of Lincoln, including without limitation administrative claims of the kind specified in 11 U.S.C. § 503(b) and §507(b), except for any administrative expense claims of Congress Financial Corporation (New England) under said §§503(b) and

507(b) (the "Congress Administrative Claims"). The Congress Administrative Claims shall at all times be senior in right of payment to the BHE Administrative Claims. For the purpose of this Order, the term Avoidance Actions shall mean causes of action of Debtors or their respective estates pursuant to Chapter 5 of the Bankruptcy Code, whether pursued by the Debtors, a trustee, the creditors committee and/or any other representative of the estate (or any successor or assignee of any of the foregoing), and all proceeds derived from the settlement, assignment and/or prosecution thereof. Except as set forth below, the BHE Administrative Claims shall not be subject to any right of counterclaim, setoff or recoupment. Notwithstanding the foregoing, in the event BHE (1) receives a Termination Payment from Sprague Energy pursuant to the terms of the Guaranty Agreement or (2) assumes the Supply Agreement and receives net revenue from the subsequent sale of electrical energy received under the Supply Agreement, the Termination Payment or net revenue shall be applied as an offset to BHE's claim against Lincoln in an amount not to exceed the amount of the Obligation (as defined in the Guaranty Agreement). Lincoln further agrees that BHE's claim based upon BHE's election under the Guaranty Agreement either to (1) assume the Supply Agreement, or (2) pay to or receive from Sprague Energy the Termination Payment (as defined in the Guaranty Agreement), shall be in BHE's sole discretion, and that Lincoln shall have no claim against BHE and no defense, right of setoff, counterclaim, or recoupment based on or arising out of BHE's election of (1) or (2), above.

3. Except as expressly provided herein, the 2001 Special Rate Agreement is hereby reaffirmed and remains in full force and effect.

4. This First Amendment is contingent upon: (1) the issuance of an Order by the Maine Public Utilities Commission unconditionally approving this First Amendment pursuant to 35-A M.R.S.A. 703 (3-A), (2) the issuance of an Order by the Maine Public Utilities Commission unconditionally approving the terms of a Stipulation entered into among BHE, Lincoln, and the Office of Public Advocate related to BHE's entrance into the First Amendment with Lincoln; and (3) issuance of an Order by the United States Bankruptcy Court for the District of Maine unconditionally approving this First Amendment. If these approvals are not obtained by the close of business on April 30, 2002, this First Amendment is null and void.

5. This First Amendment may be executed in as many counterparts as may be deemed necessary and convenient and each of which shall be deemed an original but all such counterparts shall contribute one and the same instrument.

IN WITNESS WHEREOF, the parties have caused this First Amendment to be executed

as of the date and year first written above.

WITNESS: LINCOLN PULP & PAPER CO., INC.

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By_____
Edward C. Woodbridge
Chief Financial Officer

WITNESS: BANGOR HYDRO-ELECTRIC COMPANY

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By_____

Paul LeBlanc
Vice President

GUARANTY AGREEMENT

This Guaranty Agreement is effective April 30 , 2002, by Bangor Hydro-Electric Company ("Guarantor") in favor of Sprague Energy Corp., a Delaware corporation with a mailing address of Two International Drive, Suite 200, Portsmouth, NH 03801, ("Creditor").

WHEREAS, Creditor and Lincoln Pulp & Paper Co., Inc. ("Debtor") have entered into a contract for electric generation service dated April 30, 2002 (the "Agreement"), a copy of which is attached hereto as Attachment A; and

WHEREAS, pursuant to Section 7(a) of a Special Rate Agreement between Guarantor and Debtor dated June 27, 2001, Guarantor has agreed to provide a guaranty to Creditor if so requested by Debtor, provided that Debtor has used due diligence to obtain the lowest price electric generation agreement; and

WHEREAS, Guarantor has been requested by Debtor to provide such a guaranty;

NOW, THEREFORE, for good and valuable consideration, the receipt and sufficiency of which are hereby acknowledged, Guarantor hereby agrees for the benefit of Creditor as follows:

1. Guaranty.

(a) Guarantor unconditionally guarantees to Creditor the payment of all amounts due and payable by Debtor pursuant to the Agreement (hereinafter, the "Obligation") to the extent they are not paid by or on behalf of Debtor, and the failure to make payment constitutes an Event of Default under the Agreement; provided,

however, that Guarantor is and shall be entitled to assert any and all of Debtor's claims, counterclaims, defenses, offsets and other rights against Creditor with respect to the Agreement to the extent of Guarantor's Obligation. In such event, Guarantor shall either (i) assume the Agreement for its remaining term as provided in Section 3; or (ii) pay to or receive from Creditor the Termination Payment as provided in Attachment B (the "Termination Payment"). In no event shall Guarantor be liable for any special, indirect or consequential damages.

(b) If Debtor ceases regular commercial operations at its facility in Lincoln, Maine (the "Facility") during the term of this Guaranty, for any reason, whether there is a default under the Agreement or not, Guarantor shall either (i) assume the Agreement for its remaining term, as provided in Section 3, or (ii) pay to or receive from Creditor the Termination Payment. For purposes of this Agreement, Debtor shall be considered to have ceased regular commercial operations if: (1) the Debtor becomes a debtor under chapter 7 of the Bankruptcy Code, or (2) there is a permanent cessation by the Debtor of substantially all manufacturing operations at its Facility, provided that there shall be a legal presumption, rebuttable by the Debtor, the Guarantor, or the Creditor, that any such cessation in excess of 30 consecutive days is permanent. Any dispute about the existence of such cessation shall be submitted to the Maine Public Utilities Commission (the "MPUC") in accordance with Section 7; the right to rebut any presumption shall be exercised by filing an objection with the other notified parties and the MPUC within five business days of receipt of a Shutdown Notice (as defined in 2(b) below). A Shutdown Notice shall not be considered final until the later of: (1) five business days after receipt of such notice by Debtor, or (2) in the event a party files a timely objection as provided

above, at the time the MPUC resolves such dispute and determines that Debtor has ceased regular commercial operations.

2. Claims Procedure.

(a) Payment Default. In the event Debtor defaults on the payment of any Obligation and the non-payment constitutes an Event of Default under the Agreement as contemplated in Section 1(a), Creditor shall so notify Guarantor in writing (the "Default Notice"), specifying the default with reasonable detail, with a copy to Debtor, and shall specify the amount being claimed from Guarantor hereunder.

Guarantor shall, within fifteen days after receipt of the Default Notice, (i) make such payment or cause the same to be made; and (ii) notify Creditor of its election to either assume the Agreement, as provided in Section 3 hereof, or pay to or receive from Creditor the Termination Payment. Upon receipt of Guarantor's election, Creditor shall commence deliveries to Guarantor immediately, if Guarantor elects to assume the Agreement, or Guarantor or Creditor, as appropriate, shall make the Termination Payment within fifteen days thereafter, if Guarantor elects the Termination Payment option.

(b) Shutdown of Facility. In the event that Debtor ceases regular commercial operations at the Facility as contemplated in Section 1(b), either Creditor or Guarantor shall so notify the other and the Debtor in writing (the "Shutdown Notice"), specifying any amount being claimed or, in the case of Guarantor, whether it elects to assume the Agreement. If Creditor receives the Shutdown Notice, it shall commence deliveries to Guarantor as contemplated in Section 3 after such notice becomes final, if Guarantor elects to assume the Agreement, or Guarantor or Creditor, as appropriate, shall make

the Termination Payment within 15 days thereafter, if Guarantor elects the Termination Payment option. If Guarantor receives the Shutdown Notice, it shall, within fifteen days after such notice becomes final, notify Creditor of its election to either assume the Agreement, as provided in Section 3, or pay to or receive from Creditor the Termination Payment. Upon receipt of the Guarantor's election, Creditor shall either commence deliveries to Guarantor immediately, if Guarantor elects to assume the Agreement, or Guarantor or Creditor, as appropriate, shall make the Termination Payment within fifteen days thereafter, if Guarantor elects the Termination Payment option.

3. Assumption of Agreement. In the event Guarantor elects to assume the Agreement pursuant to either Section 1(a) or Section 1(b), the terms of the Agreement shall apply to such purchases from that point forward except that all references to Lincoln Pulp & Paper Co., Inc. shall be references to Guarantor. Guarantor shall not be required to provide any further guaranty (except that Section 8 of Exhibit A to the Agreement shall apply to Guarantor) and Creditor shall deliver such generation to the interconnection point of NEPOOL's "PTF" facilities and Guarantor's delivery system that is closest to the Facility (the "New Delivery Point") ; provided, however, that Guarantor is and shall be entitled to assert any and all of Debtor's claims, counterclaims, defenses, offsets and other rights against Creditor with respect to the Agreement to the extent of Guarantor's Obligation. Creditor shall be required to deliver during each month (or portion of a month) in the Agreement assumed by Guarantor, an amount of electrical energy as determined on Attachment C attached hereto (the "Delivered Amount"). Notwithstanding any differences between the Delivered Amount and the Projected Usage (as defined on Attachment C), Guarantor's payments to

Creditor under the Agreement shall be based upon the Projected Usage. Notwithstanding the provisions of the Agreement, Creditor shall render monthly to Guarantor a billing statement showing the quantity and price of electricity delivered and any other charges as applicable for the preceding month. Guarantor shall pay Creditor the amount shown as due on each such billing statement no later than ten days after Guarantor's receipt of each billing statement. Interest shall be due on all late payments at the Prime Rate (reported by The Wall Street Journal or its successor publication), plus two percent (Prime + 2%), or the maximum legal rate if lower. Interest shall not accrue on any amount in dispute unless the dispute is resolved in favor of Creditor. Either party shall be entitled to verifiable billing adjustments requested in writing within two years of the date of the statement to be adjusted. Notwithstanding such assumption by Guarantor, Creditor shall have no right to make any claim against Guarantor as a result of the acts or omissions of Debtor (other than for amounts due in connection with Section 1(a) hereof) and Debtor shall retain all liability for such claims.

4. Term; Termination. The term of this Guaranty shall commence on the first date written above (at 12:01 a.m., Bangor, Maine time) and end on March 31, 2005 (at 11:59 p.m., Bangor, Maine time). This Guaranty may be terminated at the option of Guarantor if the Agreement is modified, amended or altered without Guarantor's written consent. This Guaranty may also be terminated, with the prior approval of both Creditor and Debtor, in the event Debtor is no longer subject to the protection of any United States Bankruptcy Court. Termination shall not affect any obligation or rights of Guarantor hereunder arising prior to the date of such termination. This Guaranty shall also terminate automatically upon payment of the Termination Payment; provided,

however, that Guarantor shall have full rights of subrogation against Debtor to the extent of any amount paid by Guarantor. In addition, any sale of the Facility to, or change in ownership of the Debtor to, an entity whose credit-worthiness is equal to or exceeds that of the Guarantor as of the date hereof, or any assignment of the Agreement, gives the Guarantor the right to terminate this Guaranty.

5. Assignment; No Third Party Beneficiaries. Neither Guarantor nor Creditor may assign its respective rights or obligations under this Guaranty without the other's written consent. Subject to the foregoing, this Guaranty shall be binding upon and inure to the benefit of the parties hereto and their respective permitted assigns and any references to such party shall mean such party or its authorized assignee. This Guaranty is for the benefit of Creditor (and, to the extent of its rights hereunder, Guarantor) only, and there shall be no third party beneficiaries to this Guaranty.

6. Notices. Any notice or other communication required to be given under this Guaranty shall be in writing, and shall be deemed to have been received on the day of delivery if delivered by hand on a business day, one business day after being sent for overnight delivery, prepaid, by Fedex or another nationally recognized express courier service, or on the fifth business day after being deposited in the U.S. Mail, registered or certified, postage prepaid, in any such case addressed as follows:

Bangor Hydro-Electric Company
33 State Street
P.O. Box 932
Bangor, Maine 04402-0932
Attention: Jeff Jones

Sprague Energy Corp.
Two International Drive, Suite 200
Portsmouth, New Hampshire 03801
Attention: James Daly

Lincoln Pulp & Paper Co., Inc.,
100 University Drive
Amherst, MA 01002
Attention: Joseph H. Torras

For purposes of this Guaranty, a "business day" shall mean a day on which the Federal Reserve member banks in New York City are open for business. Any of the foregoing parties may change its address for purposes of notice under this Guaranty by so notifying the others in accordance with the notice provisions hereof.

7. Dispute Resolution Any disputes arising under this Guaranty shall be submitted to the Maine Public Utilities Commission for adjudication and the parties agree that any decision of the Maine Public Utilities Commission shall be binding upon them.

8. Effective Date; Agreements of Debtor and Creditor. This Guaranty shall, subject to the approval of the Maine Public Utilities Commission and the United States Bankruptcy Court for the District of Maine, be effective as of the date first set forth above, but only if the respective agreements of the Debtor and the Creditor, set forth below, have been duly executed and delivered to the Guarantor.

9. Applicable Law. This Guaranty shall be governed by, and interpreted in accordance with the laws of the State of Maine, without regard to conflict of laws principles.

IN WITNESS WHEREOF, Guarantor has caused this Guaranty to be duly executed and delivered, to be effective as of the date first written above, regardless of the actual date of execution and delivery.

BANGOR HYDRO-ELECTRIC COMPANY

By:

_____

Paul LeBlanc
Vice President

Lincoln Pulp & Paper Co., Inc. (the "Debtor"), hereby agrees to notify Bangor Hydro Electric Company (the "Guarantor") immediately upon the occurrence of any default by Debtor under the Agreement (as defined above) and of any cessation of regular commercial operations at the Facility (as defined above), agrees to use its best efforts to cure any such default prior to the time that Guarantor would be required to make any payment hereunder, agrees that Debtor will be indebted to Guarantor for any amounts so paid by Guarantor (unless offset as provided for in Section 2 of the First Amendment of the Special Rate Agreement dated April 30, 2002) and that Guarantor will be fully subrogated to the rights of Creditor (as defined above) under the Agreement in the event of any such payment by the Guarantor. Debtor further agrees that Guarantor shall have the right to assume the Agreement and purchase electric generation service under the Agreement as set forth in Section 3 above. Debtor further agrees that any sale of the Facility to, or change in ownership of the Debtor to, an entity whose credit-worthiness is equal to or exceeds that of the Guarantor as of the date hereof, or any assignment of the Agreement, gives Guarantor the right to terminate the Guaranty Agreement. Debtor acknowledges that if Guarantor assumes the remaining portion of the Agreement pursuant to the terms of the Guaranty, then Debtor will no longer be entitled to the electrical energy provided under the Agreement and so will need to make arrangements for the provision of any electrical energy that it may need, whether through reliance on the standard offer or otherwise. Debtor further acknowledges that it will remain liable for all of its acts and omissions, notwithstanding any assumption by Guarantor of the remaining portion of the Agreement.

LINCOLN PULP & PAPER CO., INC.

By:

_____

Edward C. Woodbridge

Sprague Energy Corp. (the "Creditor") hereby agrees that Bangor Hydro-Electric Company (the "Guarantor") will be fully subrogated to Creditor's rights under the Agreement (as defined above) to the extent of any payment made by the Guarantor hereunder, agrees that Guarantor shall have the right to assume the remaining portion of the Agreement as set forth in Section 3 above, and further agrees to negotiate in good faith with Guarantor with respect to the Termination Payment (as defined above) and that any dispute over the amount of the Termination Payment is subject to the binding exclusive jurisdiction of the MPUC (as defined above). Creditor further agrees that any sale of the Facility to, or change in ownership of the Debtor to, an entity whose credit-worthiness is equal to or exceeds that of the Guarantor as of the date hereof, or any assignment of the Agreement, gives Guarantor the right to terminate the Guaranty Agreement.

SPRAGUE ENERGY CORP.

By:

_____

Thomas F. Flaherty

Designated Confidential Information
Maine Public Utilities Commission

ATTACHMENT A
Copy of the Supply Agreement

[Redacted]

Designated Confidential Information
Maine Public Utilities Commission

ATTACHMENT B
Calculation of Termination Payment

[Redacted]

Designated Confidential Information
Maine Public Utilities Commission

ATTACHMENT C
Delivered Amount, Projected Amount, Line Losses

[Redacted]

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