Background on Debt Optimization and Debt Service Reassignment

Background

- Beginning in Fiscal Year 2003, BPA adopted Modified Net Revenue (MNR) as a Key Agency Target to eliminate the effects of the Debt Optimization Program (DO Program) and Debt Service Reassignment (DSR) on the performance measure Net Revenues.
- The effects of the DO Program and DSR resulted in higher FCRPS Net Revenues due to debt management activities not affecting Business Unit Net Revenues.
- MNR enabled the agency to clarify the agency's position with regard to financial results based on a more representative measure of operational activities.

Debt Optimization Program Highlights

- The DO Program took advantage of debt refinancing opportunities to benefit Northwest ratepayers by refinancing (and extending) Energy Northwest debt and preserving the availability of U.S. Treasury borrowing authority by repaying Treasury debt instead.
- Because tax-exempt municipal interest rates were lower than even BPA's Treasury borrowing rates, and the fact that the program allowed BPA to issue short-term bonds to take advantage of lower interest rates, debt optimization also reduced BPA's overall interest expense.
- The goals of the program were to:
  - Restore the availability of Treasury borrowing authority.
  - Prevent any overall negative impact on rates.
  - Minimize the cost of BPA's overall debt portfolio.

Debt Service Reassignment Highlights

- Opportunities to take advantage of EN Debt refinancings under the DO Program without increasing power rates had been exhausted.
- DSR was implemented to expand the DO Program to take advantage of EN Debt refinancing opportunities by repaying transmission Treasury debt.
- The Corporate Business Unit was used as an intermediary to facilitate the accounting transactions for the DSR maintaining separate accounting as required by FERC.
- Corporate "gains" due to refinancing were recorded for the FCRPS, but were not reflected in the Power and Transmission Business Unit financial statements.
- Rates were set for each respective Business Unit as required to meet statutory and operational requirements.

Debt Service Reassignment Highlights (Continued)

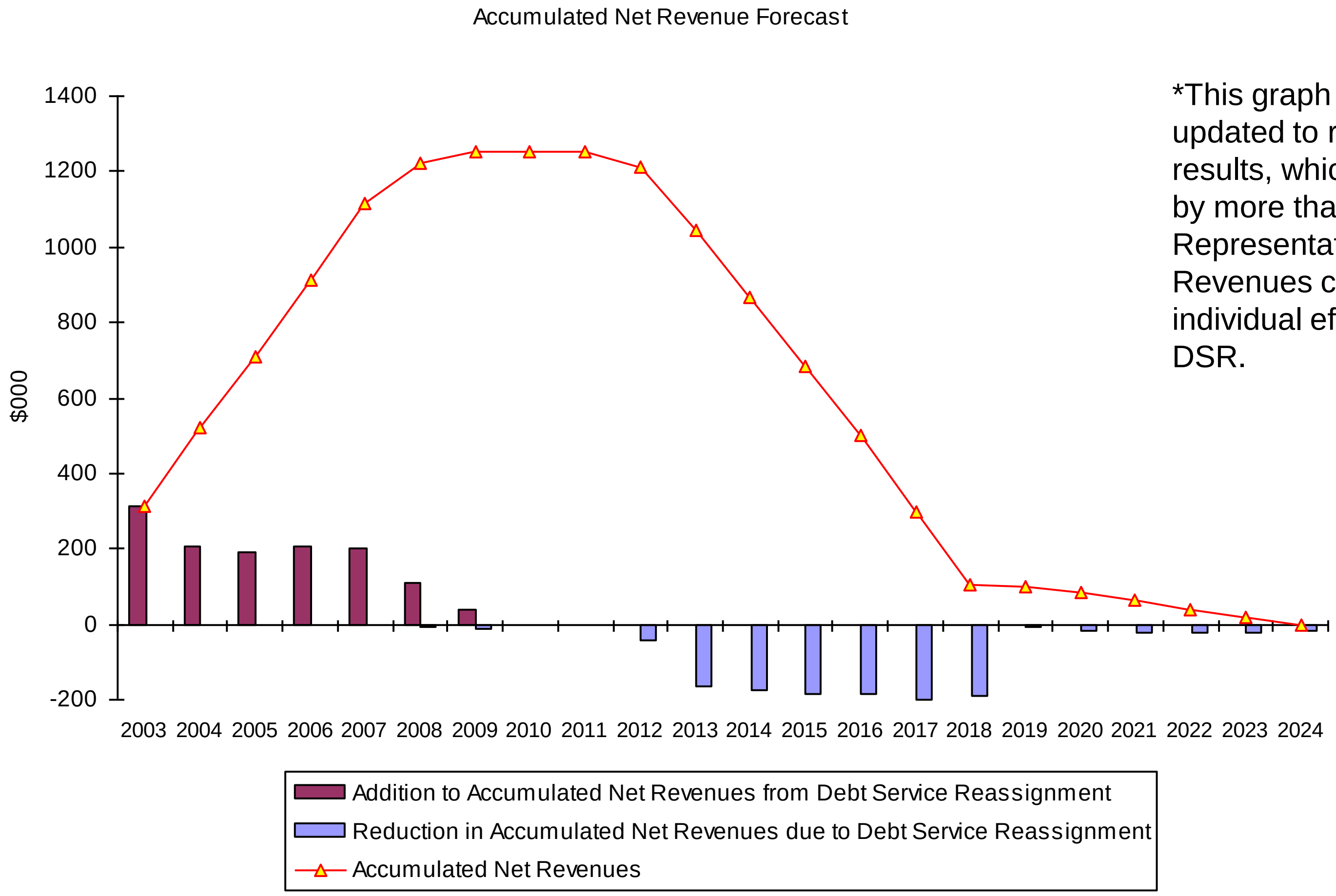
- DSR effects on Power:
  - Power repaid its obligation through rate collection.
  - For rate-setting purposes, Power rate payers are not responsible for debt service on Energy Northwest bond refinancings conducted on behalf of Transmission.
- EN debt service reassigned to Transmission is paid through Transmission rates.

Transition of Recording Debt Service Reassignment

- With the DSR construct, it was known from the beginning that the Corporate “gain” would eventually reverse when the actual EN debt service assigned to Transmission came due.
- Transmission rates, being set to recover the debt service payments through cash generated with depreciation in the revenue requirement, enables the Corporate organization to pay off the debt.
- This additional expense at the FCRPS level results in lower net revenues than is generated through the Power and Transmission Business Units.

Debt Service Reassignment Effects Over Time

- As indicated on the previous page, the effects were known to reverse over time. The following graph illustrates the effect as projected when developing the DSR construct:



*This graph has not been updated to reflect actual results, which are influenced by more than just the DSR. Representation of actual Net Revenues could mask the individual effects of the DSR.

Adjusted Net Revenue

- In an effort to eliminate the effects of DSR, the Agency has developed an Adjusted Net Revenue Key Agency Target similar to the MNR used in the past.
- Adjusted Net Revenue is calculated by adding the Power Services and Transmission Services Net Revenues.
- This calculation does not include the Corporate Business Unit Net Revenues, which eliminates the DSR debt repayment from affecting Net Revenues.
- The adjusted net revenue calculation is more reflective of day-to-day operations than FCRPS net revenues.

Illustration of Adjusted Net Revenues

- The following illustration uses the FY 2012 results to demonstrate Adjusted Net Revenues:

  ($ in thousands)

Net Revenues:

Power	Transmission	Corporate	FCRPS
$39,185	$88,710	($41,144)	$86,751

($ in thousands)	FY 2012
Power Services Net Revenues	$39,185
Plus: Transmission Services Net Revenues	$88,710
Adjusted Net Revenue	$127,895