

Management's Discussion & Analysis

Profile

The Bonneville Power Administration is a federal agency under the Department of Energy. Based in the Pacific Northwest, the agency markets wholesale electrical power from 31 federal hydro projects, one nonfederal nuclear plant and several other small nonfederal power plants. BPA also operates and maintains about three-fourths of the region's high-voltage transmission. About one-third of the electric power used in the Northwest comes from BPA. BPA is a self-funding agency that covers its costs by selling its services wholesale at cost to the region's public utilities, municipalities, investor-owned utilities and some large industries. BPA also sells or exchanges power with marketers and utilities in Canada and the western United States. Its service area includes Oregon, Washington, Idaho, western Montana and small parts of Wyoming, Nevada, Utah, California and eastern Montana. BPA promotes energy efficiency, renewable energy and new technologies. The agency funds regional efforts to protect and rebuild fish and wildlife populations affected by hydropower development in the Columbia River Basin. BPA is committed to providing public service and seeks to make its decisions in a manner that provides financial transparency and opportunities for input from all stakeholders. In its vision statement, BPA dedicates itself to providing high system reliability, low rates consistent with sound business principles, environmental stewardship and accountability. BPA's core values are trustworthy stewardship, collaborative relationships and operational excellence.

General

BPA's largely hydroelectric power supply depends on the amount of annual precipitation in the Columbia River basin and timing of the precipitation and runoff. BPA monitors the snowpack that drains into the Columbia River basin to predict each year's water and secondary energy supply. BPA assumes the lowest historical runoff as the basis for calculating its available power supply to meet its firm power obligations. BPA sells secondary energy to purchasers in the Western Interconnection at market prices when available generation exceeds what is needed to serve BPA's firm obligations. When setting power rates, BPA assumes an average level of secondary energy sales. In an average water year, BPA generally has about 1,400 to 1,600 average megawatts of secondary energy available for sale. Because precipitation and market prices vary widely, BPA builds contingencies into its rates to cover poor hydro and/or market conditions. To ensure BPA is able to meet its financial responsibilities to counterparties and to the U.S. Treasury, BPA relies on risk mitigation measures such as financial reserves and a cost recovery adjustment clause that can raise rates, if needed.

The FCRPS financial statements that follow are a combination of the accounts of BPA, the accounts of the Pacific Northwest generating facilities of both the U.S. Army Corps of Engineers and the Bureau of Reclamation as well as the operation and maintenance costs of the U.S. Fish and Wildlife Service for the Lower Snake River Compensation Plan Facilities. Consolidated with BPA are "Special Purpose Corporations" known as Northwest Infrastructure Financing Corporations, from which BPA leases certain transmission facilities.

Results of Operations

Operating Revenues

For the six months ended March 31, 2009, revenues decreased \$92 million, or about 6 percent from the comparable period a year earlier, as reported in the Combined Statements of Revenues and Expenses. Power Services revenues declined \$117 million, or 9 percent. The decline is the result of reduced revenues from surplus sales due to the combination of below-average precipitation and lower prices for surplus sales, lower priority firm power rates for preference customers, and the return of approximately \$35 million of Residential Exchange Program Lookback Amounts as credits on preference customers' power bills. The 2007 Supplemental Wholesale Power Rate Case Final Record of Decision was issued on Sept. 22, 2008. The Final ROD established the Lookback Amount, representing BPA's overpayments to investor-owned utilities from prior years, which was also the amount over-collected from preference customers. Lookback Amount credits on preference customer bills started Oct. 1, 2008. Transmission Services sales increased \$13 million, or 4 percent, mainly due to ancillary services. Ancillary services are those services that are necessary to support the transmission of capacity and energy from resources to loads while maintaining reliable operation of BPA's Transmission System in accordance with good utility practice. The ancillary services variance was primarily due to within-hour balancing for resources because it was a new product this year and its comparison was to zero revenues last year and energy and generation imbalance.

The increase in the unrealized fair value of BPA's derivative instruments of \$29 million was due to fluctuations in the forward prices curves, physical delivery and a change in the overall portfolio mix. The change was primarily the result of delivery of power contracts.

U.S. Treasury credits for certain fish and wildlife expenditures incurred by BPA decreased \$4 million, or 9 percent, due to decreased market prices for replacement power purchases largely driven by lower natural gas prices.

Operating Expenses

Operations and maintenance increased \$57 million, or 8 percent for the six months ended March 31, 2009, from the comparable period a year earlier due to scheduled maintenance and biennial refueling of the Energy Northwest Columbia Generating Station nuclear power plant in fiscal year 2009.

Purchased power expense decreased \$39 million, or 17 percent, due to lower market prices, in spite of a higher volume of purchases.

Nonfederal projects expense increased \$8 million, or 3 percent, primarily due to higher amortization for Energy Northwest's Columbia Generating Station. During both periods, restructured nonfederal debt enabled the early repayment of federal debt in lieu of nonfederal debt amortization. When compared to the six months ended March 31, 2008, less debt was restructured under debt optimization in the six months ended March 31, 2009. Refer to modified net revenues below.

Net Interest Expense

For the six months ended March 31, 2009, interest expense increased \$4 million, or 2 percent, for the six months ended March 31, 2009, from the comparable period a year earlier. The primary drivers were increases arising from the Lease Financing Program and customer advances for transmission construction. Allowance for funds used during construction increased \$6 million, or 51 percent, with the primary drivers being increases for the Lease Financing Program, customer advances for transmission construction and BPA direct funded projects. Interest income increased \$0.7 million, or 2 percent due to higher cash balances.

Liquidity and Capital Resources

Net Revenues and Operating Activities

As a result of the factors previously discussed, the FCRPS earned net revenues of \$34 million for the six months ended March 31, 2009. By comparison, net revenues were \$123 million for the six months ended March 31, 2008.

Cash provided by operating activities of the FCRPS decreased \$259 million to \$165 million for the six months ended March 31, 2009, when compared to the comparable period a year earlier, as reported in the Combined Statements of Cash Flows. The change in operating cash flow reflects the changes in net revenues, net of the impact of changing derivative values, and differences in the timing of collecting receivables and payments of accounts payable and accrued liabilities. The net change attributable to the Residential Exchange Program was a \$251 million outflow.

Investment Activities

Cash used for investment activities of the FCRPS increased \$192 million to \$404 million for the six months ended March 31, 2009, when compared to the six months ended March 31, 2008. The change in investment activities is primarily driven by BPA's investment of \$100 million under a new agreement with the U.S. Treasury under which BPA purchased investment securities referred to as "market-based specials." BPA plans to invest an incremental \$100 million each year for up to 10 years or until the Bonneville Fund is fully invested in Treasury securities.

During the six months ended March 31, 2009, the consolidated special purpose corporations deposited \$176 million into their restricted trust funds and advanced \$85 million to the Bonneville Fund to support transmission construction activities on leased projects. This represents a net outflow of \$62 million when compared to the same activity for the six months ended March 31, 2008.

Financing Activities

Cash provided by financing activities of the FCRPS was \$207 million for the six months ended March 31, 2009, compared to \$40 million for the comparable period a year earlier. Increases to nonfederal debt and customer advances for transmission construction were partially offset by repayment of borrowing from the U.S. Treasury.

Non-GAAP Financial Information

Modified Net Revenues

Management has determined that modified net revenues are a better representation of the outcomes of normal operations during periods of debt management actions and fluctuations in derivative market prices. Modified net revenues are net revenues after removing the effects of derivative instruments and nonfederal debt management actions that differ from rate case assumptions.

Modified net revenues were \$105 million lower for the six months ended March 31, 2009, compared to the comparable period a year earlier, primarily due to the decline in net revenues previously discussed.

The table below demonstrates the calculation for modified net revenues.

Modified Net Revenues

Federal Columbia River Power System

For the fiscal year-to-date ended March 31 — thousands of dollars

	2009	2008
Net revenues	\$ 34,067	\$ 122,570
Derivative instruments	35,023	64,432
Nonfederal debt management actions	(57,643)	(70,062)
Modified net revenues	\$ 11,447	\$ 116,940

Additional Information

To see BPA's most recent annual report including audited financial statements, go to www.bpa.gov/corporate/finance/a_report

To see BPA's news, go to www.bpa.gov/corporate/BPAnews

For general information about BPA, refer to BPA's Home page at www.bpa.gov

For information on Power Services including rates, go to www.bpa.gov/power

For information on Transmission Services including rates, go to www.transmission.bpa.gov

For information about hydro power or current hydrological information, go to www.bpa.gov/power/pgf/hydrology/weekly.shtml

Federal Columbia River Power System Combined Balance Sheets

(Unaudited)

March 31,
2009

September 30,
2008

(thousands of dollars)

Assets		
Utility plant		
Completed plant	\$ 13,553,710	\$ 13,480,633
Accumulated depreciation	(5,008,965)	(4,933,348)
	8,544,745	8,547,285
Construction work in progress	990,840	890,883
Net utility plant	9,535,585	9,438,168
Nonfederal generation	2,487,535	2,492,645
Current assets		
Cash	1,699,243	1,731,238
U.S. Treasury market-based special securities	14,580	-
Accounts receivable, net of allowance	103,153	112,129
Accrued unbilled revenues	204,730	203,011
Materials and supplies, at average cost	80,837	75,719
Prepaid expenses	26,051	21,682
Total current assets	2,128,594	2,143,779
Other assets		
Regulatory assets	5,357,560	5,447,404
U.S. Treasury market-based special securities	83,625	-
Nonfederal nuclear decommissioning trusts	145,807	157,743
Deferred charges and other	258,097	176,045
Total other assets	5,845,089	5,781,192
Total assets	\$ 19,996,803	\$ 19,855,784

Capitalization and Liabilities		
Capitalization and long-term liabilities		
Accumulated net revenues	\$ 2,698,527	\$ 2,664,460
Federal appropriations	4,282,348	4,247,972
Borrowings from U.S. Treasury	1,660,500	1,745,500
Nonfederal debt	6,348,416	6,182,403
Total capitalization and long-term liabilities	14,989,791	14,840,335

Commitments and contingencies (See Note 10 to annual financial statements)

Current liabilities		
Federal appropriations	9,889	9,889
Borrowings from U.S. Treasury	500,400	440,400
Nonfederal debt	284,934	284,469
Accounts payable and other	549,725	588,275
Total current liabilities	1,344,948	1,323,033
Other Liabilities		
Regulatory liabilities	2,605,839	2,665,517
IOU exchange benefits	70,763	69,600
Asset retirement obligations	159,000	159,800
Deferred credits	826,462	797,499
Total other liabilities	3,662,064	3,692,416
Total capitalization and liabilities	\$ 19,996,803	\$ 19,855,784

Federal Columbia River Power System
Combined Statements of Revenues and Expenses
(Unaudited)

	Three Months Ended March 31,		Fiscal Year-to-Date Ended March 31,	
	<u>2009</u>	<u>2008</u>	<u>2009</u>	<u>2008</u>
(thousands of dollars)				
Operating revenues				
Sales	\$ 746,627	\$ 807,963	\$ 1,473,145	\$ 1,565,008
Derivative instruments	4,924	(48,313)	(35,023)	(64,432)
U.S. Treasury credits for fish	22,224	25,167	43,814	48,122
Miscellaneous revenues	18,497	14,806	33,430	32,245
Total operating revenues	792,272	799,623	1,515,366	1,580,943
Operating expenses				
Operations and maintenance	400,067	345,323	750,257	692,889
Purchased power	69,201	97,581	192,591	231,422
Nonfederal projects	130,706	125,145	254,658	246,418
Depreciation and amortization	88,491	89,034	176,492	177,565
Total operating expenses	688,465	657,083	1,373,998	1,348,294
Net operating revenues	103,807	142,540	141,368	232,649
Interest expense and (income)				
Interest expense	82,286	79,874	163,598	159,726
Allowance for funds used during construction	(9,365)	(5,860)	(17,507)	(11,567)
Interest income	(19,828)	(19,551)	(38,790)	(38,080)
Net interest expense	53,093	54,463	107,301	110,079
Net revenues	\$ 50,714	\$ 88,077	\$ 34,067	\$ 122,570

Federal Columbia River Power System

Combined Statements of Cash Flows

(Unaudited)

Fiscal Year-to-Date Ended
March 31,

2009

2008

(thousands of dollars)

Cash provided by and (used) for operating activities

Net revenues	\$	34,067	\$	122,570
Non-cash items:				
Depreciation and amortization		176,492		177,565
Amortization:				
Terminated facilities and sponsored conservation		4,605		4,385
Capitalization adjustment		(32,453)		(32,452)
Changes in:				
Receivables and unbilled revenues		7,257		(12,435)
Materials and supplies		(5,118)		(7,420)
Prepaid expenses		(4,369)		(5,441)
Accounts payable and other		(15,010)		178,192
Cash provided by operating activities		165,471		424,964

Cash provided by and (used) for investment activities

Investment in:				
Utility plant (including AFUDC)		(214,185)		(184,039)
Nonfederal generation		5,110		4,930
U.S. Treasury market-based special securities		(100,000)		-
Nonfederal nuclear decommissioning trusts		(3,924)		(3,559)
Special purpose corporations' trust funds:				
Deposits to		(176,192)		(37,720)
Receipts from		85,133		8,429
Cash used for investment activities		(404,058)		(211,959)

Cash provided by and (used) for financing activities

Federal construction appropriations:				
Increase		34,376		40,943
Repayment		-		-
Borrowings from U.S. Treasury:				
Increase		95,000		95,000
Repayment		(120,000)		(115,000)
Refinanced		-		(20,000)
Nonfederal debt:				
Increase		176,193		37,720
Repayment		(9,715)		(9,315)
Customers:				
Advances for construction		34,208		14,647
Billing credits		(3,470)		(4,263)
Cash provided by financing activities		206,592		39,732
(Decrease) increase in cash		(31,995)		252,737
Beginning cash balance		1,731,238		1,475,544
Ending cash balance	\$	1,699,243	\$	1,728,281