

# FINANCIAL RESERVES POLICY

## 1. Background and Purpose

The Financial Reserves Policy (Policy) provides a consistent, transparent, and financially prudent method for determining BPA's target ranges for financial reserves available for risk (financial reserves). The Policy establishes upper and lower financial reserves thresholds for Power Services, Transmission Services, and the agency as a whole, which define the target ranges. The Policy also describes the actions BPA may take when financial reserves levels either fall below a lower threshold or exceed an upper threshold. The Policy supports BPA's requirement to establish the lowest possible rates consistent with sound business principles.

Prior to the Policy, BPA did not have a consistent way to establish financial reserves target ranges and upper and lower financial reserves thresholds for each business line and BPA. This is of particular importance because financial reserves levels and financial reserves policies and practices have a direct effect on BPA's credit rating, which is determined at the aggregate BPA level. BPA, however, sets rates to recover costs for each business line individually. The lack of a consistent policy across the business lines and for BPA as a whole allows for *ad hoc* financial reserves decisions and different treatment for each business line.

Establishing prudent financial reserves lower thresholds over time for the business lines helps to maintain BPA's credit rating, solvency, and rate stability, which is consistent with sound business principles. Establishing prudent financial reserves upper thresholds for the business lines and BPA as a whole ensures that financial reserves do not grow to unnecessarily high levels but rather are invested back into the business or distributed as rate reductions, both of which lower revenue requirement costs.

## 2. Scope of the Financial Reserves Policy

The Policy affects financial reserves available for risk (financial reserves) attributed to Power Services (Power) and Transmission Services (Transmission).

The Policy establishes lower and upper financial reserves thresholds for Power Services and Transmission Services, and upper financial reserves thresholds for the agency at the ends of fiscal years. The Policy also provides guidance on the actions BPA should take when financial reserves fall below established lower threshold levels or rise above established upper threshold levels at the ends of fiscal years.

The Policy does not preclude or hinder in any way the Administrator's authority to use financial reserves for purposes deemed necessary by the Administrator.

The Policy is intended to provide a consistent framework within which BPA can manage its financial reserves. To that end, the Policy will constitute precedent that BPA will adhere to in future rate cases absent a determination by the Administrator that the Policy must be modified to meet BPA's changing operating environment.

### **3. Financial Reserves Thresholds**

#### **3.1 Definitions**

**Financial reserves available for risk.** Financial reserves available for risk (financial reserves) consist of cash, market-based special investments, and deferred borrowing, all of which are highly liquid and unobligated for BPA to use to mitigate financial risk, less any outstanding balance on the Treasury Facility.

**Days Cash on Hand Metric.** Days cash on hand is the number of days a business can continue to operate using its own cash on hand with no new revenue. Days cash on hand is a common industry liquidity metric measuring the relationship between the amount of cash a business holds and the amount of average daily expenses incurred in operating the business.

#### **3.2 Business Line Financial Target Ranges**

Financial reserves target ranges for each business line shall be calculated independently each rate period, and consist of upper and lower financial reserves thresholds, which define the upper and lower ends of the target ranges.

#### **3.3 Lower Financial Reserves Thresholds**

Lower financial reserves thresholds shall be calculated independently for Power and Transmission each rate period based on the greater of: (1) 60 days cash on hand, and (2) what is necessary to meet the Treasury Payment Probability (TPP) Standard. For each business line, if financial reserves fall below the lower threshold, a rate action shall trigger the following fiscal year to recover, in part or in whole, the shortfall.

#### **3.4 Upper Financial Reserves Thresholds**

Upper financial reserves thresholds shall be calculated independently for Power and Transmission each rate period and will be the financial reserves' equivalent of 60 days cash on hand above the lower financial reserves thresholds. The agency upper threshold is the sum of Power and Transmission's lower thresholds plus 30 days cash on hand for the agency.

##### **3.4.1 Financial Reserves Distributions**

If business line financial reserves and agency financial reserves are above their respective upper thresholds, the Administrator shall consider the above-threshold financial reserves for investment in other high-value business line-specific purposes including, but not limited to, debt retirement, incremental capital investment, or rate reduction.

### 3.5 Calculation of Lower and Upper Financial Reserves Thresholds

<b>3.5.1 - Power Services</b>		
Power lower financial reserves threshold	=	The greater of: (1) 60 days * (Power operating expenses / 365 days), and (2) the threshold needed to achieve a 95% TPP.
Power upper financial reserves threshold	=	Power lower financial reserves threshold plus 60 days * (Power operating expenses / 365 days)
<i>Where:</i>		
Power operating expenses	=	Power total expenses - (Power depreciation and amortization + Power net interest expense + Power non-federal debt service + Power purchases)

<b>3.5.2 - Transmission Services</b>		
Transmission lower financial reserves threshold	=	The greater of: (1) 60 days * (Transmission operating expenses / 365 days), and (2) the threshold needed to achieve a 95% TPP.
Transmission upper financial reserves threshold	=	Transmission lower financial reserves threshold plus 60 days * (Transmission operating expenses / 365 days)
<i>Where:</i>		
Transmission operating expenses	=	Transmission total expenses - (Transmission depreciation & amortization + Transmission net interest expense)

<b>3.5.3 - Agency</b>		
Agency upper financial reserves threshold	=	The sum of the Power lower financial reserves threshold and the Transmission lower financial reserves threshold plus 30 days cash on hand for the agency
<i>Where:</i>		
30 days cash on hand for the agency	=	30 days * (agency operating expenses / 365 days)
Agency operating expenses	=	Power operating expenses + Transmission operating expenses

## 4. Implementation

### 4.1 Overview

The Policy will be implemented each rate period through the Power and Transmission rate schedules and GRSPs. The lower and upper financial reserves thresholds for each business

line will be recalculated each time BPA establishes new Power and Transmission rates. Lower and upper financial reserves thresholds will remain constant throughout each rate period. Lower and upper financial reserves thresholds will be computed using forecast rate period average operating expenses from the Power and Transmission revised revenue tests.

Implementation shall include parallel rate mechanisms for each business line each rate period that will trigger if financial reserves are below the lower financial reserves thresholds. Implementation shall also include parallel Financial Reserves Distributions for each business line each rate period that will trigger if financial reserves are above upper financial reserves thresholds.

## **4.2 Provisions for Increasing Financial Reserves**

The methodologies for increasing financial reserves are described below. The specific rate mechanisms to achieve 4.2.1 through 4.2.3 will be determined in the applicable rate proceeding.

4.2.1 Except as provided in section 4.2.2, if financial reserves attributable to a business line are below its lower threshold, then the annual rate action will be the lower of the following two, unless a larger increase in reserves is necessary to achieve the TPP standard:

- (1) \$40 million per year in Power rates, if recovering Power financial reserves; \$15 million per year in Transmission rates, if recovering Transmission financial reserves; or
- (2) the amount needed to fully recover financial reserves up to the applicable business line lower threshold.

4.2.2 The \$40 million per year rate action described above in section 4.2.1(1) is being phased in for Power until Fiscal Year (FY) 2022. In FY 2022 and thereafter, the \$40 million per year rate action in section 4.2.1(1) will apply and this section 4.2.2 will be inapplicable. In FY 2020 and FY 2021, if financial reserves attributable to Power are below its lower threshold, then the annual rate action will be the lower of the following two, unless a larger increase in reserves is necessary to achieve the TPP standard:

- (3) \$30 million per year in Power rates; or
- (4) the amount needed to fully recover financial reserves up to the Power lower threshold.

4.2.3 In addition to the rate action described above in sections 4.2.1 and 4.2.2, Bonneville will initially propose in each rate case a rate mechanism to increase each business line financial reserves in the event they fall below \$0. Such rate mechanism will include the following parameters:

- (1) When financial reserves are below \$0 for Power Services, Bonneville will recover in each year of the rate period the first \$100 million dollar-for-dollar.

Bonneville will recover only fifty cents on the dollar for any amounts greater than \$100 million. This provision will be limited to an annual cap of \$300 million; and

- (2) When financial reserves are below \$0 for Transmission Services, Bonneville will recover in each year of the rate period the first \$100 million dollar-for-dollar. This provision will be limited to an annual cap of \$100 million.

Implementation of the methodology described above, including the timing of when the calculations in (1) and (2) will be performed, will be determined each rate period through the Power and Transmission rate schedules and GRSPs. Such implementation may include *de minimis* thresholds.