Decision Support
Resolving Major Financial Policy Issues

E.1 Working capital requirements/reserve assumptions: Calculation, use, and tracking Business Line (BL) reserves

Since this item addresses two distinct areas that are not exclusive to one recommendation that fits the proposals, the "calculation" and "tracking" are identified separate from the "use" of BL reserves.

E.1.a. – Calculation and tracking BL reserves.

<u>Summary of Issues:</u>

- Historically, calculations of BL reserves have been based on an analysis of pre-BL physical separation separate accounting as required by the Federal Energy Regulatory Commission (FERC). This methodology is based on analysis of rate case fictionalization information and FCRPS actuals to identify those costs recovered through rates for the generation and transmission functions.
- Post-BL physical separation, Bonneville has developed cost structures and allocations to assign and report specific costs and revenues to each of the BL's providing the ability to separately report financial activity. However, with only one BPA fund with Treasury it has not been prudent to extend this separation to record reserves and cash balances by BL.
- As a substitute for recording actual reserves and cash by BL, tracking of BL reserves has been based on an annual analysis of BL Statement of Revenue and Expense reports with adjustments for accrual to cash transactions and other information pertinent to identifying surrogate BL cash and reserve balances.
- Recently, in order to address concerns raised as to the reliability of an annual reserve calculation, Financial Operations has identified a methodology to allocate total cash to BLs. This methodology uses a monthly calculation to capture the seasonal trends of cash flows for each of the BLs, providing a more reasonable approach to end of year reserve calculations. BPA began tracking both the monthly net cash flows and ending cash balance on a business line basis. The methods used to track the cash flows by business line are recorded, understood, and recalculable by others. The other aspect of reserve calculations entail the idenfication of deferred borrowing by BL. Tracking borrowing by business line is BPA's current practice, so that is not at issue.
- Although BPA currently tracks both cash and borrowing on a business line basis, it does not track reserves on a business line basis. Instead BPA tracks reserves on an agency basis.
- Since this is a new methodology, concerns have been raised as to the validity of the beginning cash and reserve balances developed from the previous methodology and accuracy of the calculations. Additionally, concerns have been raised whether the new methodology will withstand rate case scrutiny and acceptance due to a changed methodology.
- Concerns have also been raised regarding the rate case, Treasury Payment Probability (TPP), and Safety Net Cost Recovery Adjustment Clause (SN CRAC) implications if PBL and TBL introduce separate business line reserves into their rate cases. Currently, the TPP is an agency TPP that impacts the SN CRAC trigger, which is a PBL rate mechanism.

<u>Strategic Context—Related Agency and BL Strategic Objectives:</u>

E.1.a - Calculation and tracking BL reserves

[redacted]

Alternatives to be Considered:

1. Maintain status quo – Methodology based on initial Business Line reserves calculated as of 9/30/02, with adjustments to annual Business Line Net Revenues incorporating accrual to cash adjustments.
2. Track business line reserves using the methods currently in use and approved by Financial Operations. Refer to separate business line reserves during rate cases.

Evaluation of Alternatives against Key Decision Criteria:

Alternative 1 - Maintain status quo – Methodology based on initial Business Line reserves with adjustments to Business Line Net Revenues incorporating accrual to cash adjustments.

1. Business/Finance
   - **Liquidity – 2 – No effect on agency liquidity**. A less precise calculation based on adjustments to Business Line Net Revenues may result in higher or lower reserve balances for a particular Business Line that may influence rate designs resulting in rate impacts that could impact liquidity. We believe there are no direct impacts on agency liquidity.
   - **Flexibility – N/A –** Annual calculations or monthly calculations will not impact financial flexibility.
   - **Impact on Sustainable Capital Access - N/A –** Annual calculations or monthly calculations will not adversely impact sustainable capital.
   - **Cost Shifts Across Rate Periods – 3 – No shifts discernable**. A less precise calculation based on adjustments to Business Line Net Revenues may result in higher or lower reserve balances for a particular Business Line that may influence rate designs resulting in rate impacts that could impact rates across periods. Less precision may change the outcome of the reserve levels from other methodologies; however, we do not believe there is a shift across rate periods resulting from the calculation and tracking reserves.
   - **Cost Shifts Between Groups – 3 – No shifts discernable.** A methodology based on adjustments to Business Line Net Revenues may result in higher or lower reserve balances for a particular Business Line that may influence rate designs resulting in rate impacts that could impact rates across periods. Less precision may change the outcome of the reserve levels from other methodologies; however, we do not believe there is a shift between groups resulting from the calculation and tracking reserves.
   - **Cost Recovery – 2 – No effect on ability to recover costs.** Although reserve levels are part of the rate computations that result in cost recovery, we do not believe the reserve calculation methodology will have any impact on cost recovery efforts.
   - **Rate Impacts – 2 – Policy has no likely effect on reaching rate targets.** Although reserve levels are part of the rate computations, we do not believe the calculation methodology and use will have any impact on rates.
   - **Impact on Risk Profile – 2 – Has no effect on either financial volatility or overall risk exposure.** Although the overall reserve number calculated may be part of BPA's overall risk equation, we do not believe the calculation methodology has an effect on risk exposure.
2. Public Responsibility

[redacted]

- **Likelihood of agreement by Administration – 3 – Able to reach agreement with minimum effort.** We do not believe that the administration will take issue with the calculation of reserves, however, we believe given a choice of a more accurate approach would be favorable to them.
- **Likelihood of agreement by external partners – 3 – Able to reach agreement with minimum effort.** We do not believe that the external parties will take issue with the calculation of reserves, however, we believe given a choice of a more accurate approach would be favorable to them.
- **Likelihood of support by customers/constituents – 3 – Supported by all.** Since the calculation methodology has been used in prior rate proceedings, we do not believe customers or constituents would take issue with this methodology.
- **Potential for leading to less financially prudent actions –3 – Not at all likely**. Since the calculation methodology has been used in prior rate proceedings, we do not believe the calculation will enable a degradation of efforts in other areas or lead to less accurate calculation methodologies in the future.

3. Environmental
   - **Likelihood that policy will enhance BPA role as environmental steward in the region – 3 – No harmful impacts perceived**. There are no anticipated impacts resulting from the calculations of reserve balances by business line.

[redacted]

5. People and Culture
   - **Ease and/or expense of implementation – 3 – No increase or reduction, business as usual.** Since the methodologies utilize existing processes, there are no additional impacts to workload.
   - **Clarity of Direction – 3 – Virtually complete buy-in by employees, integrity of decision unquestioned.** Since the calculation methodology has been used in prior rate proceedings, we do not believe there will be any additional learning required.

Alternative 2 - Track business line reserves using the methods currently in use and approved by Financial Operations.

1. Business/Finance
   - **Liquidity – 2 – No effect on agency liquidity**. With the accuracy improvements in assigning reserve levels for business lines, there are no direct impacts on agency liquidity.

[redacted]

- **Flexibility – N/A –** Although the calculation will provide more accurate measure of Business Line reserves, we do not believe this decision materially impacts other decisions or actions.
- **Impact on Sustainable Capital Access - N/A –** Although the calculation will provide more accurate measure of Business Line reserves, we do not believe there are any implications for capital or capital access.
- **Cost Shifts Across Rate Periods – 3 – No shifts discernable**. With a more accurate approach to assigning reserve levels, we believe there are no rate period cost shifts resulting from the calculations. Although the level of reserves may have an impact on proposed rates, the calculation method does not impact overall reserve levels. More accuracy may change the outcome of the reserve levels from other methodologies; however, we do not believe there is a shift across rate periods resulting from the calculation, use and tracking reserves.
- **Cost Shifts Between Groups – 3 – No shifts discernable**. With a more accurate approach to assigning reserve levels, we believe there are no cost shifts between groups resulting from the calculations. Although more accuracy may change the outcome of the reserve levels from other methodologies, we do not believe there is a shift across customer groups.
- **Cost Recovery – 2 – No effect on ability to recover costs.** Although reserve levels are part of the rate computations that result in cost recovery, we do not believe the reserve calculation methodology and use will have any impact on cost recovery efforts.
- **Rate Impacts – 2 – Policy has no likely effect on reaching rate targets.** Although reserve levels are part of the rate computations, we do not believe the calculation methodology and use will have any impact on rates.
- **Impact on Risk Profile – 2 – Has no effect on either financial volatility or overall risk exposure.**

2. Public Responsibility
   - **Likelihood of agreement by Administration – 3 – Able to reach agreement with minimum effort.** Since the calculation is based on a methodology that provides more accuracy through month-to-month analysis of cash for determining reserve levels, we do not believe external partners would take issue with this methodology
   - **Likelihood of agreement by external partners – 3 – Able to reach agreement with minimum effort.** Since the calculation is based on a methodology that provides more accuracy through month-to-month analysis of cash for determining reserve levels, we do not believe external partners would take issue with this methodology.
   - **Likelihood of support by customers/constituents – 3 – Supported by all.** Since the calculation is based on a methodology that provides more accuracy through month-to-month analysis of cash for determining reserve levels, we do not believe customers or constituents would take issue with this methodology.
   - **Potential for leading to less financially prudent actions –3 – Not at all likely**. Calculations of reserve levels engrained in month-to-month transaction analysis will not enable a degradation of efforts in other areas or lead to less accurate calculation methodologies in the future.
3. Environmental

[redacted]

- **Likelihood that policy will enhance BPA role as environmental steward in the region – 3 – No harmful impacts perceived**. There are no anticipated impacts resulting from the calculations of reserve balances by business line.

[redacted]

5. People and Culture
   - **Ease and/or expense of implementation – 3 – No increase or reduction, business as usual.** Since the methodologies utilize existing processes, there are no additional impacts to workload.
   - **Clarity of direction – 3 – Virtually complete buy-in by employees, integrity of decision unquestioned.** Since the calculation methodology is an improvement over what has been used in prior rate proceedings, we do not believe there will be any additional learning required.

Summary Table – E.1.a.

Decision Criteria	Alternative 1 Annual Approach	Alternative 2 Monthly Approach
Liquidity	2	2
Flexibility	N/A	N/A
Sustainable Capital	N/A	N/A
Rate Period Cost Shift	3	3
Customer Group Cost Shift	3	3
Cost Recovery	2	2
Rate Impact	2	2
Impact on Risk Profile	2	2
Administration Agreement	3	3
External Partner Agreement	3	3
Customer Support	3	3
Potential Imprudent Actions	3	3
Environmental Impact	3	3
[redacted]	[redacted]	[redacted]
[redacted]	[redacted]	[redacted]

[redacted]

Unfavorable Precedent	3	3
Ease of Implementation	3	3
Clarity of Direction	2	2

Recommended Resolution:
Track business line reserves using the methods currently in use and approved by Financial Operations. Refer to separate business line reserves during rate cases.

Schedule and Forum for Decision:
March 17, 2004: Prepare and deliver to the Steering Committee PRELIMINARY Alternative descriptions and evaluation for all issues using criteria along with 2-sentence description for each criterion explaining the rationale for the evaluation and the source(s) of the risk.
April 7, 2004: Present 2nd draft alternatives and evaluations, along with team recommendations on E and F - Working Capital and Financial Risk. Steering Committee concurs or expresses different expectations with respect to the recommendations and evaluations.
April 21, 2004: Present FMC presentation package to Steering committee for review.
April 27, 2004: FMC review and approval of financial policy decisions for the rate cases

Responsible Lead Manager:
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