

BONNEVILLE POWER ADMINISTRATION

LEARNING FROM THE FINANCIAL CRISIS: BPA AT A CROSSROADS

**A REPORT TO THE ADMINISTRATOR
PREPARED BY
THE INTERNAL REVIEW TEAM**

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PART 1 - INTRODUCTION

In 2002 BPA began assessing the causes of a gap between its expected financial results in the FY 2002-2006 rate period and forecasts of those results made during the 2000 rate case. Actions to close the gap have transformed BPA from an agency with relatively low power rates and large financial reserves to one with much higher rates and smaller reserves. On January 7, 2003, the Administrator formed an internal review team to interview employees about reasons for the gap and what BPA can learn about better delivering on its mission in the future.

While the team's initial assignment was to focus on the period since May 2000, many of those interviewed traced origins of the financial gap back to at least the mid-1990's. Part 2 below covers the background they discussed as context for the remaining sections of the report. The team conducted 72 interviews with staff, management and executives, and analyzed the results to identify major themes and conclusions that best represent what was learned through the interviews (see methodology in Attachment 1). These themes and conclusions are presented in Part 3. The team took a holistic view of the interview results and its knowledge of BPA to develop recommendations for BPA's consideration, as shown in Part 4.

PART 2 – INTERVIEW BACKGROUND

In the mid-1990's, and for the first time in its history, BPA power rates exceeded the market price of wholesale power. Although BPA lost some customer load to the market, most of the Federal system capability remained under long-term contract until 2001. However, BPA knew it could face serious financial consequences if existing customers chose not to renew their contracts when they expired in 2001. Early in 1996, Pacific Northwest governors convened a Comprehensive Review of the Northwest Energy System to seize opportunities and moderate risks created by the transition of the region's power system to a more competitive electricity market. They appointed a Steering Committee of power system stakeholders to study and make recommendations on the system's transformation. Regarding BPA's future role, this Comprehensive Review established primary goals of:

1. Aligning the benefits and risks of access to existing Federal power.
2. Ensuring greater probability of repayment of debt to the U.S. Treasury while not compromising the security or tax-exempt status of BPA's third-party debt.
3. Retaining the long-term benefits of the system for the region.

The Steering Committee recommended that BPA use a subscription based system to allocate Federal system electricity, and also recommended that BPA not acquire additional resources to serve expanded loads except on a bilateral contract basis, when the customer absorbed the risk.

By 1999, BPA was well on its way to achieving the goals of the Comprehensive Review. A portion of the Federal system had already been re-contracted on a long-term basis through pre-subscription contracts, market prices had recovered to a level at or above BPA's costs, and a string of good water years had brought positive financial performance and increased reserves.

Further, BPA had begun turning away from a role of acquiring resources for the region by dismantling its load forecasting, resource acquisition, and other functions.

Early in 1999, the BPA Administrator told the Northwest Power Planning Council: (1) analysis showed 2000-2001 operating year deficits of almost 2,500 MW for 80 percent of Septembers and 3,800 MW for 36 percent of Februarys (out of the record of 50 water years), and (2) since most of the imbalance was on the non-Federal system, BPA was not planning to meet that load. Yet, in May 2000, prior to completion of the subscription process, BPA announced a new five-year average priority firm rate of \$22 per MWh. The rate case assumed that the load on BPA would exceed the system's capability by 1,700 aMW; BPA analysts thought that amount could easily grow to 2,400 aMW. This load was not limited in magnitude or constrained by timing.¹ When 3,300 aMW above system capability was subscribed in November 2000, the stage was set for the marketplace and other factors to hammer BPA's financial and rate goals.

Interview discussions covered a series of key decisions that, in aggregate, have taken BPA down a very different path than that laid out in the Comprehensive Review recommendations. These decisions were never accompanied by a deliberate reconsideration and redirection of BPA's post-2001 role, either within BPA or among regional stakeholders. They include decisions to:

- Offer a below-market priority firm rate for all subscription load;
- Use cost estimates in the rate case that many analysts and managers viewed as too low;
- Rely on an unprecedented level of secondary energy sales revenues;
- Establish five-year rather than two-year rates;
- Use cost recovery adjustment clauses (CRACs) whose impacts were not fully understood;
- Cap rates for pre-subscription contracts and/or exempt them from the CRACs;
- Agree on a Residential Exchange program settlement that substantially increased costs;
- Augment resources to cover most of the over-subscription ahead of the rate period; and
- Use flat, five-year purchases/buy-downs for most of that augmentation.

Today, BPA looks much different than the agency envisioned by the Comprehensive Review. Financial reserves are depleted and BPA's ability to make the fiscal-year-end Treasury payment is far from certain. Distribution of Federal system benefits has changed dramatically in ways not anticipated in May 2000. The amount paid to investor-owned utilities has increased by nearly 600 percent to over \$400 million per year. Rates for nearly 1,000 MW of public customer load (pre-subscription) are under \$22 per MWh, but rates for other preference customers are already up more than 45 percent and will increase again under the safety net CRAC. Further, the many sub-products and rates, the complexity of the Slice contracts, and the multiple CRACs have sometimes overwhelmed the capabilities of BPA's systems and staff.

PART 3 - INTERVIEW THEMES AND CONCLUSIONS

Interviews were conducted against the backdrop of the events and decisions listed above. They indicate why many interviewees concluded that BPA's actions played a large part in its current financial crisis, although the negative results were amplified as BPA decisions played out against

¹ Under the expiring contracts, utilities had to provide notice of up to 7 years before returning load to BPA.

the drought of 2000-2001 and the California market experience. Many believe that BPA made a set of decisions starting in the 1990's that made it highly unlikely it could fulfill regional stakeholders' vision from the Comprehensive Review or deliver on rate case expectations.

Interviewees discussed events, decisions and activities that they participated in or had knowledge of during the period of the mid-1990's to January 2003. From this background, they noted what they believe has caused or contributed to the current situation and where BPA can improve. Through data analysis, the team identified the most common themes across the 72 wide-ranging interviews and distilled each theme into more specific conclusions. Causal factors discussed below are, in the opinion of those who raised them, still operative and need corrective action going forward, even though the event/decision/activity that shows the need may be in the past.² Four major themes cover the changes needed for BPA to improve its future results:

- Theme 1: Long-term outcomes for business and public values need to guide BPA.
- Theme 2: Aspects of BPA's cultural base that hinder long-term outcomes need to be addressed.
- Theme 3: BPA's business infrastructure needs to better support its business objectives.
- Theme 4: Decision-making in support of long-term outcomes needs improvement.

Theme 1: Long-term outcomes for business and public values need to guide BPA.

This theme was raised in a variety of ways by roughly two-thirds of those interviewed. Many saw it as foundational to gaining improvements under the other themes. The conclusions are:

- Staff and management lack a coherent picture of the future BPA is trying to create, including a clear understanding of long-term outcomes and the strategies to reach them.
- Executives and managers need to be guided in their decision-making by long-term outcomes and strategies, rather than by short-term goals.
- We can build political understanding and support around clearly articulated long-term outcomes.

Conclusion 1: Staff and management lack a coherent picture of the future BPA is trying to create, including a clear understanding of long-term outcomes and the strategies to reach them.

Many interviewees at all levels -- staff, managers, and executives -- discussed what they consider to be lack of clarity about what BPA is trying to create, what specific outcomes are sought in the long term, and what strategies are being used to reach those outcomes. They can't articulate BPA's long-term plan and can't place many individual decisions into a proper context. Indeed,

² Interviews included the four basic questions in Attachment 1, and generally did not allow time to solicit views among interviewees on the relative pros and cons of specific corrective actions discussed by each interviewee.

they are often confused by apparently conflicting decisions and management actions that don't add up to a coherent long-term picture. One such conflict was using rate case costs that assumed a hydro-resource-based role and simple contracts while taking on a regional supplier role and entering complex Slice contracts. Another involved not monitoring/managing to the "aggressive cost targets" as far as possible once they were used in the rate case. Yet another was taking on a regional supplier role, but using a flat, highly load-attracting rate, rather than a tiered rate.

Conclusion 2: Executives and managers need to be guided in their decision-making by long-term outcomes and strategies, rather than by short-term goals.

Many interviewees described how the lack of long-term outcomes and strategies too often leads to a short-term focus in responding to pressures from customers and the marketplace. Decisions guided by, and aligned with, long-term outcomes could help avoid adverse results such as interviewees see in the current inability to raise pre-subscription contract rates that were capped, or to reduce benefit payments to investor-owned utilities that were fixed for the entire rate period.

Conclusion 3: We can build political understanding and support around clearly articulated long-term outcomes.

Interviewees discussed how stakeholder interests impact BPA's ability to develop a clear picture of what it is trying to create and to set long-term outcomes toward that future state. A number expressed a belief that BPA can build stakeholder understanding and support for well-defined long-term outcomes that benefit the region as a whole by proposing a business model and working with the region to help shape it. They said BPA could do more to help customers see the importance of maintaining our financial viability.

Theme 2: Aspects of BPA's cultural base that hinder long-term outcomes need to be addressed.

Nearly all interviewees raised this theme in some way, often noting how critical it is to truly examine BPA's culture and determine how changes can be accomplished. The conclusions are:

1. A few critical executive and managerial competencies need to be strengthened.
2. We often avoid accountability, self-criticism, and acknowledgment of mistakes.
3. Important information, insights, and perspectives that challenge conventional wisdom frequently are not encouraged or explored.

Conclusion 1: A few critical executive and managerial competencies need to be strengthened.

A clear majority of interviewees discussed this theme and raised at least four competencies: business acumen, understanding risk and uncertainty concepts, managerial courage, and managing and measuring work for results. Interviewees said that key decision-makers and managers at all levels need to strengthen their business acumen -- the ability to understand and focus on business drivers, financial principles and economic fundamentals, and to tie operational alternatives

and impacts to those factors. They cited examples of decisions they believe did not show adequate understanding among decision-makers of the financial issues and impacts or marketplace and economic realities involved.

Interviewees believe decision-makers need to more fully comprehend and apply risk concepts, as shown by two opposite responses that create sizeable risks: trusting in uncertain events to cover very certain costs, and requiring certainty at increased cost. They saw such responses in BPA choosing to tie secondary sales forecasts to prices far above prior levels in a volatile market, and basing most of its augmentation on flat, non-displaceable purchases when the hydro system has lost much of its ability to shape power to load. Interviewees sense that, if executives and managers better understood risk management concepts, they would put more value on capturing risk exposure in staff analyses. Some expect the recent enterprise risk management study to eventually raise risk management competencies BPA-wide.

Many interviewees said that there is an unwillingness to stand up and be the only champion for an idea, possibly because “rocking the boat” is perceived as career limiting. Some believe the need for increased managerial courage was evident in managers not engaging the front office on the widespread view that rate case cost estimates would be very difficult to achieve.

Interviewees at all levels indicated that BPA managers need to improve their ability to exercise the disciplined management required to develop plans and keep them on track. They noted that, after making decisions, managers may take inadequate steps to manage to those decisions, and may fail to decide in advance how success will be measured or to follow through later and determine whether an effort was successful or not. One example noted was the Slice program. Following the decision to offer Slice, no steps were taken to assure the Slice development team received necessary internal cooperation and input until negotiations with customers were too far along to make significant changes. Also, while Slice really amounts to a pilot program, no criteria were set to evaluate its success.

Conclusion 2: We often avoid accountability, self-criticism, and acknowledgment of mistakes.

Many interviews discussed cultural shortcomings surrounding accountability and results measurement. Accountability is viewed as being largely about results: knowing if a person, program or function is successful or not; determining who or what is responsible for a failure, learning how to improve an organization; and recognizing/celebrating true successes (i.e., those that meet pre-determined success measures).

Many interviewees said that de-emphasis or avoidance of accountability is reflected in several aspects of BPA’s culture. For example, having many strategic objectives/thrusts and not clarifying their relative priorities and interactions allows actions in practically any direction to appear supportive of targets and objectives, and makes true accountability almost impossible. Also, manager contracts with many performance items and few points assigned to each item were seen as an accountability problem since success might be judged and rewarded based on meeting a high percentage of contract targets, while the most critical items are not accomplished. Finally, a broad de-emphasis of accountability is reflected in not routinely comparing outcomes of key de-

cisions to expectations and applying lessons learned to future situations. And, when there is data pointing to an alternative course, there is rarely any comparison of decision results with those expected under the alternative in order to identify possible improvements in the decision process.

Conclusion 3: Important information, insights and perspectives that challenge conventional wisdom frequently are not encouraged and explored.

A majority of interviewees perceive that opinions differing from the desired course of action or challenging conventional thinking are frequently not valued or probed for understanding, and that sometimes they are even discouraged. Some noted that counter positions are not sought out, and that when they are listened to, the purpose may be to exclude rather than to understand what the person is saying. They also said that sometimes it appears a decision-maker is so confident of the answer, he/she sees no need to probe.

Theme 3: BPA's business infrastructure needs to better support its business objectives.

Interviewees at all levels clearly perceive that BPA's business infrastructure can be improved to better support its business objectives. Their conclusions are that BPA needs to:

1. Organize for more efficient and effective support of business objectives.
2. Improve control of business processes and procedures.

Conclusion 1: Organize for more efficient and effective support of business objectives.

Interviewees said that some staff resources are not organized in an efficient or effective manner to support our current business needs. They noted that BPA's efficiencies projects currently underway could result in improvements for some functions such as information technology services, but that analytical or other functions may still need attention. Over the past eight years, while market complexity grew and BPA adopted more complex rates and CRACs, analytical functions such as load forecasting, market intelligence, and rates were downsized or disbanded altogether. Moreover, the remaining analytic capability is scattered across the agency. This has diluted the analytical voice and has contributed to sometimes-inconsistent analysis as different groups start with different assumptions and bases.

Conclusion 2: Improve control of business processes and procedures.

Interviews pointed to the need to improve control of processes and procedures in many areas of BPA's business to better assure they support business objectives. The suggested improvements generally involve either better separation of duties and more appropriate delegation of authorities, or greater standardization of business processes and reports.

Separation of duties and delegation of authorities

Several interviewees saw a need to better separate trading from other duties. Assuring accurate accounting was one concern: trades moved from one "book" to another, or a string of related trades not appropriately linked, can skew results and give an inaccurate picture of how trades are

performing against targets. Many interviewees had concerns about how authorities have been delegated in some areas of the business, particularly those involving contracting and payment functions. They cited account executives' and traders' waiver of amounts due BPA to settle bills and AE's modification of customer contracts with effects on timing of cash flows as two areas where authority is sometimes used without consultation with financial staff or adequate management reporting to reduce risks and assure oversight.

Standardization of business processes and reports

Interviewees also discussed the need to standardize many of BPA's business processes and reports so they align with and better support the business objectives. They noted that, in interacting with the Bonneville Enterprise System, many business processes reflect personal choices of a manager or employees, and result in duplicative spreadsheet-based systems, nonstandard inputs to BES, and unreliable management reports from the system. Also, many analytical processes are seen as ad hoc with little standardization on use of assumptions/databases, thereby causing excessive time spent in questioning the validity of analysts' numbers. Finally, several interviewees said that lack of clarity on long-term outcomes, strategies, and management plans leads to uncertainty about the kind of reports managers need to successfully manage to their objectives.

Theme 4: Decision-making in support of long-term outcomes needs improvement.

Many interviews dealt with the need to improve the decision-making process in order to better serve executive, managerial, and staff requirements. Three conclusions were drawn:

1. Objectives of key decisions must be more fully understood and stated.
2. Our decision processes should more adequately explore the costs and risks of alternatives as they relate to our business outcomes.
3. We must improve the presentation of our analysis and the information flow between analysts and decision-makers.

Conclusion 1: Objectives of key decision must be more fully understood and stated.

Interviewees discussed situations in which decision-makers thought they made reasonable decisions, but where unintended results now plague BPA. Many said such problems begin with not asking what we are trying to accomplish and not clearly documenting the answers. They believe that clearly describing the decision objective(s) can reveal any "ready . . . fire . . . aim" issues, can help determine how decisions relate to one another in support of long-term outcomes, and can help identify the costs and risks of decision alternatives to overall BPA operations.

Conclusion 2: Our decision processes should more adequately explore the costs and risks of alternatives as they relate to our business outcomes.

Discussions noted that decision processes (1) include cost and risk analyses that are insufficient in scope, (2) don't reflect an enterprise wide risk management structure and process, and (3) of-

ten lack adequate time for informed decision-making. Several interviewees said that rate case analyses have never been accompanied by a risk analysis showing the probability of certain events and the potential cost/risk of those events. They said an improved rate case would include a complete risk and cost analysis associated with the different scenarios, ascertaining outcomes that lie in the risk tails and developing explicit contingency plans to deal with such outcomes. They noted that, for some decision processes, the scope of the analysis should include the costs or risks involved in implementing alternatives in BPA's highly political environment.

Many interviewees discussed BPA's lack of an enterprise wide risk management structure and process directed by a corporate risk manager who can assure decision processes properly consider relevant risks. Some current processes may include risk analysis, but the analysis does not consider BPA-wide risk, or often fails to evaluate important potential scenarios. Some interviewees noted that BPA plans to implement an enterprise risk management organization and specific risk analysis provisions that may minimize or eliminate many of these concerns.

Many interviewees said BPA's environment often gives managers little time to reflect on data analyses and to understand interrelationships of issues and financial implications of major policy calls. They said BPA should cultivate an environment where full exploration of risk and uncertainty is valued and required before key decisions are made.

Conclusion 3: We must improve the presentation of our analysis and open the information flow between analysts and decision-makers.

Analysts and decision-makers are often frustrated by ineffective communications with each other. Analysts said their inputs are often ignored. Managers said they are often overwhelmed with analyses that are difficult to sort through, and that the reasons for their decisions are misunderstood and the decisions unjustly criticized. Improvement ideas included: (1) informing analysts of the kind of information decision-makers need to make decisions, (2) standardizing and centralizing the decision process and communications to present a robust risk and cost analysis and majority/minority views, and (3) informing analysts of decisions when they are made.

PART 4 - RECOMMENDATIONS

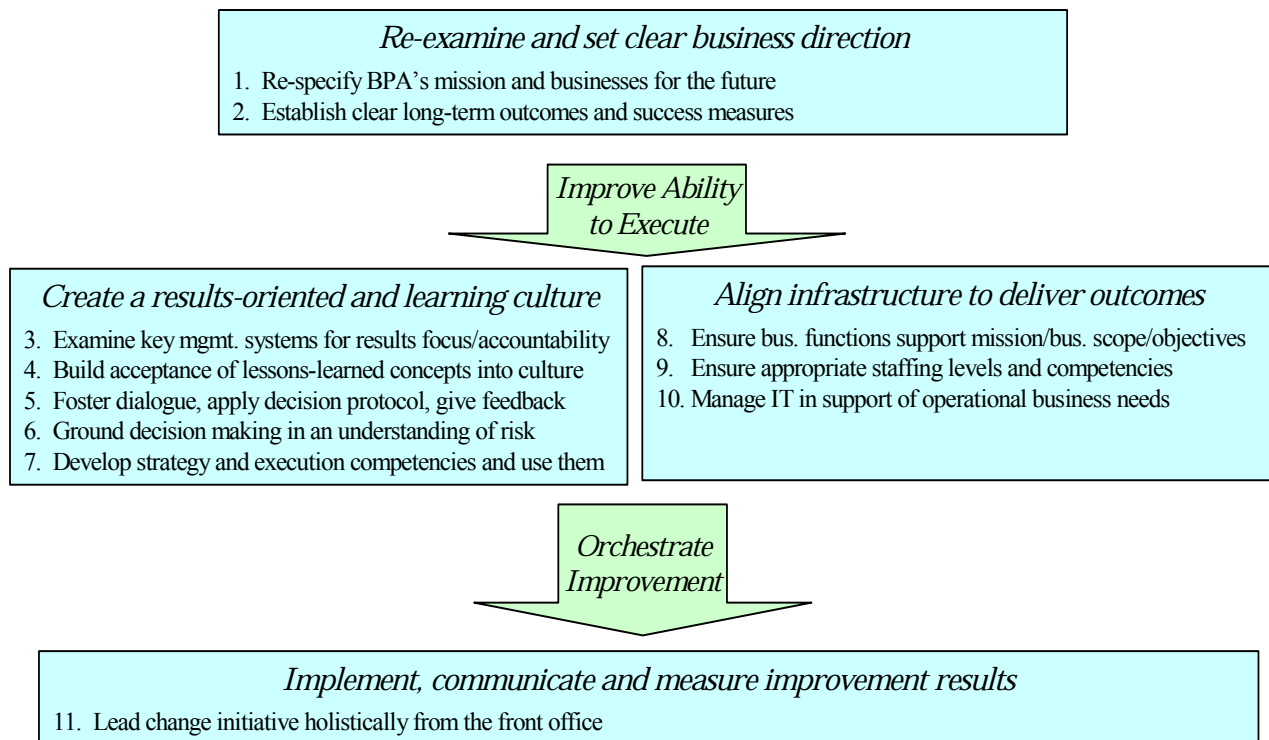
The interviewees, a cross-section of staff, managers and executives primarily from the Power Business Line and Corporate, present an amazingly consistent view: BPA is at a crossroads. They believe that now is the time to re-examine the very essence of BPA's ability to deliver public benefits. They are proud of the agency's past accomplishments but believe that we must make fundamental changes in some aspects of the way we do business to avoid the type of outcomes we are now experiencing and to strengthen the agency for the future.

Recommendation Framework

The team created a recommendation framework that does not require agreement with all the specifics of the conclusions, yet squarely addresses the major themes in four basic action areas:

- Re-examine and set clear business direction
- Create a results-oriented and learning culture
- Align infrastructure to deliver outcomes
- Implement, communicate and measure improvement results

Recommendation Framework



BPA has considered and adopted improvement actions in virtually every area of this framework within the past 10 years, often gaining valuable insights and achieving positive results. One need go back no further than the 1990's to understand this. The agency's response to deregulation began with bold moves in many areas -- creation of account executives; significant cost reductions; competitive positioning of its products; and use of management systems such as the SBOs, manager contracts, and rewards/recognition to communicate, track and reinforce results. Yet, the discipline of consciously examining results, learning for improvement and taking adaptive action is not engrained in our culture. It is reasonable to summarize the general messages of the interviews as: (1) vision and strategy are either not understood or not articulated in a complete and coherent way, (2) there is not a consistent focus on results, and (3) positive and negative consequences associated with outcomes are not the norm. While BPA often has had the "right idea"

and displayed “moments of brilliance” in developing improvement initiatives, unfortunately it hasn’t always effectively executed the concepts.

The essence of our recommendations is clearer business direction with improved organizational execution. It is a message that calls for everyone -- not just executives, not just management, but everyone -- to improve their efforts at understanding what we are trying to achieve for the region, and to execute their responsibilities with a vigorous focus on producing agency results.

Re-Examine and Set Clear Business Direction

Nearly all interviewees reflected on BPA’s mission and business strategy, and while their terminology was often inconsistent, staff, managers, and executives alike pointed to a lack of clarity in business direction. The team understands that BPA’s organic statutes both help and hinder understanding its mission. BPA is given broad latitude to provide value to the region. The underlying source of the economic value is clear. That value derives from the difference between low cost supply and delivery of power products, and the market value of these products. But BPA provides other values as well. As a public body, decision-making can be much more open and engaging of stakeholders. We are able to make investments in conservation, renewable resources, the environment and the cultural resources of the region. Our statutes give us wide discretion to provide value so long as our actions reasonably relate to the underlying objective of providing reliable, economic and environmentally sound power and transmission services. However, the balance among these other values and the rates we charge may be less well understood. The sustainability of the current balance may even be in question.

BPA’s mission statement says it “exists to meet its public responsibilities through commercially successful businesses.” It acknowledges that commercial business success is essential to deliver on the full range of public values BPA provides. However, as current issues related to the RTO, Slice, rate setting, subscription contracts, augmentation, conservation, renewable resources, fish and wildlife funding, current financial conditions, etc. grow in magnitude and importance, people are left wondering just what business we are in to deliver on what public values. They understand that the picture of the future cannot be precise, but feel a need for better direction.

Recommendation 1: Re-specify BPA’s mission and business for the future.

With all the external pressures and conflicting expectations, now is the time for BPA to re-examine and re-specify its mission for the future. This re-examination and re-specification is the foundation for all that follows, and it should not be shortchanged. Clear questions should be asked and answered that explore the full range of options. For example, does BPA simply market from the existing FCRPS resources? Does it provide value by serving load in excess of the FCRPS? Is BPA the region’s renewable resource developer and supplier? And so on. The implications of such alternatives must be explored from all angles. Although executives tend to have a high tolerance for ambiguity and understand that the right timing for making key decisions is critical, this same ambiguity creates confusion and organizational dysfunction. Therefore, the sooner a more focused picture of our future direction is created, the better. The Regional Dialogue presents both a challenge and an opportunity to obtain this more focused picture.

Recommendation 2: Establish clear long-term outcomes and success measures.

Once clear mission and business choices are made, developing measurable long-term outcomes would give staff a better understanding of what they can do to help create success. The outcomes must reflect the true value that the agency is committed to providing to the region. They must be sufficient in number to capture the drivers, but not so many as to dilute their ability to provide strategic and management guidance. These same outcomes both derive from and create the political understanding of the agency. The outcomes can be the unifying element for BPA and the region.

It is likely that some people within the agency will ask the question: “Don’t our SBOs fulfill this recommendation?” The answer is “yes and no”. First, in spite of the SBOs existence, the interviewees did not feel they have sufficient guidance and understanding. Our conclusion is that, although most of the SBOs make sense, they don’t provide long-term measures that allow people to understand the gap they should be closing. Consider SBO 3: “Be a low-cost provider of power . . . in the region.” The organization’s efforts will be decidedly different with “ultimate” targets of \$22 per MWh versus \$28 per MWh. And it is important not only to specify the target, but the rationale for it and how that target fits with the SBOs.

While having a clear understanding of the mission and expected outcomes is essential, it does not ensure success. Reflecting on BPA’s past experiences, it is clear that significant cultural and organizational changes are needed around the idea of excellence in execution

Create a Results-Oriented and Learning Culture

The conclusions section of this report suggests that the culture does not sufficiently support excellence in business execution: we need to be more business and results oriented, adhere to procedures and take individual accountability.

Recommendation 3: Examine the key management systems to ensure that they are tied to long-term outcomes, are results-oriented and designate accountability.

Once the mission, outcomes and vision are more clearly described, each organizational unit can think, plan and take appropriate action to close the gap between a forthright assessment of the present situation and the desired future. The concepts appear simple, almost simplistic. But the trick is to execute with commitment throughout the organization: top down and across each unit. One of the most frequent messages from the interviews relates to the need for more disciplined management systems. In some cases, the management systems in the form of specific processes do not exist. In other situations, the management systems exist but it is not apparent that the processes drive the business, that all units use them effectively or that there are consequences for good or poor results and/or non-compliance.

An example for understanding this recommendation is the application of the balanced scorecard. The BSC is a state-of-the-art system for aligning processes and resources to achieve long-term outcomes. Although most organizational units have a BSC on paper, very few use it to detect developing issues, to assess progress and to make mid-course corrections. We don’t currently

use the BSC to help us face issues head on for the purpose of improvement. There is a direct connection between this recommendation and the next one.

Recommendation 4: Build acceptance of lessons learned concepts into the culture.

The team recommends three steps towards building acceptance of lessons-learned concepts into the culture. First, cultivate behaviors that support an improvement mentality: individuals and the organization openly face issues, regularly address problems as systems issues (not to find fault or blame), increase appreciation for and understanding of what it means to find root-causes, and accept the importance of measuring results. Second, build lessons-learned thinking and formal key-decision review processes into the way we work. That is, when key decisions are made set a date for assessing results. At that time, ask what we have learned from either successes or failures, and develop appropriate tools to incorporate those learnings. This step does not envision adding a department. Instead, the training group could redirect its efforts and management could create expectations by establishing decision assessment dates. Third, consciously apply the learning to the next applicable situation.

Finally, while the team commends executive management for commissioning this study and requesting recommendations, it is the effectiveness and sustainability of the follow-up actions that will be the basis by which this project is judged. A visible, planned and systematic lessons-learned follow-up initiative would go a long way to convincing staff that senior management is serious about organizational improvement.

Recommendation 5: Foster open dialogue, apply a standard protocol to ensure a holistic consideration of options, and give feedback on rationale for key decisions.

In dialogue with various executives, it was clear that a partial information vacuum created many of the concerns staff expressed about decision-making. That is, executives in fact did consider a wide variety of opinions and options, but often did not close the loop with those people who were involved in the decision process to explain their rationale in terms of expressed long-term outcomes or other factors. In other cases, it is not clear that all of the options that were explored at lower levels surfaced to the decision-makers, or were presented in ways that allowed the decision-maker to understand the consequences of the decision. Interviewees want to feel that their ideas are being truly explored for understanding at appropriate stages of the process rather than debated in a win-lose environment. It is incumbent on supervisors, managers and executives to ensure that forums exist that foster this exploration.

Encouraging an open dialogue and the surfacing of diverse approaches backed by data is the foundation for good decisions. The team believes that a formal key decision process would serve the needs of executives, managers and staff. Requiring that decision papers review all reasonable options -- including their pros and cons and the risks and potential consequences in terms of long-term outcomes -- would assure staff and managers that their points of view were considered and allow executives to see the whole picture. Developing a process and habit of closing the loop by explaining the rationale for the decision to those who provided input would go a long way toward aligning support within the organization for strong execution.

Recommendation 6: Ground decision making in an understanding of risk.

In BPA, there is a limited understanding of risk concepts, how to analyze risk and assess potential consequences. Nearly all interviews reflected on some aspect of risk management. Whether the notion of short-term versus long-term, lack of clear outcomes, optimistic assumptions, etc., all came back to the consequences to the business. Failure to address this was seen as a primary reason for BPA's current financial crisis and as an impediment to any sustained improvement in our ability to deliver on long-term outcomes. Strengthening this skill-set is of prime importance. Formal training for those involved in risk decisions and development of standard risk analysis procedures under BPA's enterprise risk management process are recommended.

Recommendation 7: Develop strategy and execution competencies and use to select, promote and assign personnel.

Data from the interviews indicate that the following competencies need to be strengthened within the agency: creating vision and purpose, business acumen, managerial courage, strategic agility, quality decisions including risk assessment (as discussed above), and managing through systems.³ The competencies identified link directly to the key themes of the report: clarify strategy and improve execution. The team identified creating vision and purpose in the often-mentioned concern for understanding agency direction. The rest of the list goes to increasing our individual capability to turn strategy into reality to achieve results.

The team was particularly struck by repeated interview comments relating to business acumen. People used this term to cover business fundamentals, external drivers, and the integration of internal business and people systems to drive results. To the interviewees, it did not appear there is sufficient understanding of how decisions impact the financials.

BPA has a sophisticated development assessment and development planning process. However, as confirmed by the HR Learning staff, we do not have a strong culture of development and personal growth, except for technical enhancement. We have all the state-of-the-art processes and tools, but lack evidence of regular managerial follow-up on progress or revision of plans to recognize improvement or changed needs.

Examples of alternatives for applying the recommendation are:

1. Performance reviews. Include as a part of all annual performance reviews a section that requires each person to present his or her improvement plan and describe how his or her performance has improved as a result of new learnings.
2. Business training. Since most managers come to BPA as public servants rather than business operators, it may pay dividends to train them in the intricacies of financial management and computer simulation for "operating" an energy business. This could be accomplished at little or no additional cost by refocusing BPA's current training functions to include a BPA Management Academy, making use of non-BPA instructors in business man-

³ See Attachment 2 for working definitions of these terms.

agement and finance. BPA top leaders should be active academy participants in dialog with trainees about BPA's business outcomes and strategies.

Align Organizational Infrastructure to Deliver the Long-Term Outcomes

Recommendation 8: Ensure business functions support mission, business scope and objectives.

Interviewees said BPA should support its mission, business scope, and objectives through more effective organization of its business functions and better control of its business processes and procedures. The disconnect between the role BPA plays and the organization that supports that role was noted in functions such as load forecasting and resource planning, whose elimination in the 1990's corresponds to a business scope in line with the Comprehensive Review, rather than the business BPA seems to be in. Also, the functional management of risk is not aligned with the exposure BPA faces. It has been nearly a decade since BPA made the type of disciplined, top-to-bottom review of its business functions that every organization periodically needs to assure direct support for its mission and business. Intervening changes, including those now being contemplated, have been primarily piecemeal. Future changes need to be driven by a clear view of the mission and desired long-term outcomes.

Effective pursuit of business objectives demands effective control of business processes and procedures. Key components of control such as delegation of authority, separation of duties, and standardization of processes, databases and reports, need to be examined and improved. One or more of these components should be reviewed for functions such as marketing and sale of power and transmission services, functions that regularly interact with BES, analytical functions, and budgeting and other management oversight functions. Priority for reviewing business controls should begin with functions and processes considered most essential in supporting the business mission, scope and long-term outcomes, and/or those that subject BPA to the greatest risks.

Recommendation 9: Ensure appropriate staffing levels and competencies.

In the nearly ten years since BPA last reviewed staffing levels and instituted a conscious downsizing to align with its view of its mission and desired outcomes, significant changes have occurred. Deregulation is better understood. BPA's role has changed. The consequences of risk are more obvious. Many change initiatives have been started. The need for and capability of technology has advanced. In the end, the tie between staffing levels, competencies, and the long-term outcomes may have been lost.

An industry best practice is to make use of specialty consultants to review staffing levels and competencies. Such reviews help to ensure that the logic of the individual decisions that have led to the current staffing does not cloud the assessment of what is needed to accomplish the business today and in the future. Benchmarking business functions can also help clarify the appropriateness of current staffing compared to others performing similar functions. BPA must be prepared to respond to the findings with appropriate tools to align staffing levels and competencies with needs.

Recommendation 10: Manage information technology in support of business needs.

The evolving energy market and other factors have increased the need for effective management oversight of sophisticated IT systems and systems development. BPA's steps in this direction include initiating an Enterprise Architecture Strategy in FY 2001 for lifecycle management of information system development, investment monitoring and asset management; and beginning to re-engineer the agency-wide business of IT in FY 2002 to improve processes for consistent IT investment, and improved accountability for scope, cost and schedule. BPA's IT efforts need to be managed under an IT plan that is driven by business needs and long-term outcomes. The plan should: (1) review current systems to ensure that they support the business functions, (2) work toward elimination of system and tool duplication, and (3) ensure IT project management includes project tracking and accountability for cost and schedule.

BPA also needs to redesign and standardize aspects of its business processes that involve use of BES and other key IT systems in order to better support long-term outcomes for the business. For these systems, actions paralleling those that KPMG Consulting recommended for BES in a FY 2002 study are needed. The actions need to ensure that, wherever practical in meeting business requirements, leading practices are used, duplicative databases and data warehouses are reduced or eliminated, and standard data definitions, data input, and reporting are employed.

Implement, Communicate, and Measure Improvement Results

Much of what the team heard brings into question the agency's ability to forthrightly assess itself, to learn from its past performance and to incorporate those learnings into the fabric of BPA to improve its future performance. Importantly, data from other internal surveys indicate that BPA is not skilled at managing work for results. Nevertheless, the interviewees expect significant change. To increase the likelihood of successful implementation, the team believes BPA must respond to this report in a manner that demonstrates clear commitment to and accountability for improvement. The time frames for change must be realistic. Fundamental change such as this may well require 3 to 5 years of dedicated work, perseverance and monitoring of results.

Recommendation 11: Lead change from the front office.

The prior ten recommendations are synergistic in how they reinforce one another. They also constitute a major change initiative to be led by the front office and engaged by the entire agency, rather than a series of individual recommendations with scattered responsibility and possibly no accountability. The team believes that, if the executives don't lead this effort, it won't happen; if the whole agency does not engage, the results won't occur. This initiative should be seen as one of the most important efforts in the agency and be accorded appropriate visibility, staffing, and management and executive time and attention. The Administrator should establish a senior project manager reporting to the front office and charged with clear objectives. The project manager, perhaps with the assistance of a steering committee, should establish clear measures and targets and an action plan drawn from the conclusions and recommendations and other sources. The progress against the measures and targets must be reviewed quarterly and reported to the agency. Because of the need to improve BPA's accountability for change and its execution skills, the team suggests that additional means of keeping the change process visible and ac-

countable be developed. For example, semi-annual check-ins with the internal review team and a survey of interview participants might be ways to gain another perspective on results being achieved. After each check-in, assess the need for and make any necessary course changes. Consciously and publicly remove any barriers to implementation.

Attachment 1**Methodology**

The team was asked to complete the interviews in about a two-week period so tentative results would be available by January 31. In the interviews, the team used four questions aimed at a free-flowing discussion of the reasons for the changing financial results and any “lessons learned” about things BPA needed to do better or things that worked well:

1. What are the main reasons why BPA rate case expectations for stable rates and large reserve levels have not been met?
2. What are the causes involved for each of the reasons you mentioned?
3. Are there any lessons learned about things BPA might do differently in the future?
4. Are there any lessons learned about things that worked well?

The team selected interviewees to give a broad cross-section of staff, managers, and executives who were either directly involved in, or closely aligned with, rate setting, power marketing, financial management, and related activities. A total of 72 interviews were held, involving 14 executives, 17 managers, and 41 staff. The interviewees represented the Power Business Line (44), Corporate (21), the Transmission Business Line (4), and BPA’s front office (3). Interviews were usually held by team member pairs, but in a few cases, by the entire team. Interviewees were encouraged to be candid and were assured that any specific comments used in reporting results would not identify the source. Virtually all interviews lasted at least an hour, with many extending to two hours or more.

To analyze the tentative interview results, team members began by identifying key points made by each interviewee. These were used in facilitated team workshops to create affinity groups that revealed the most commonly discussed topics, to select those statements that best represented each group, and to assess the data in additional ways to identify major themes and conclusions interviewees made under each theme. A non-BPA facilitator helped the team assure it was consistently objective in portraying what the interviews showed rather than what team members might think about the interview results.

Finally, the team developed recommendations for BPA to consider in responding to the improvement needs raised by the interviewees. In this last step, the team took a holistic view of the interview results and its own knowledge of BPA to move from themes and conclusions to recommended actions. This was essential because very few interviews afforded enough time for thorough discussion of specific actions the interviewee might recommend to realize the needed improvement he or she identified for the team.

Attachment 2**Competency Definitions**

- **Business acumen:** Focus on business fundamentals, drivers, and the integration of the business elements.
- **Managerial courage:** Willing to stand alone, to be the only champion for an idea or position on difficult issues.
- **Political savvy:** Maneuvering through complex stakeholder issues, understanding where landmines are and being able to accommodate multiple views that fit the business requirements.
- **Strategic agility:** Sees ahead, anticipates future trends and consequences that yield sound strategies and plans.
- **Quality decisions:** Makes good decisions based on mixture of analysis, experience, wisdom and judgment that stand the test of time.
- **Managing and measuring work through systems:** Understanding and using processes, procedures and systems to manage and monitor the business without personal intervention.
- **Creating vision and purpose:** Developing and communicating a compelling and inspired sense of core purpose.