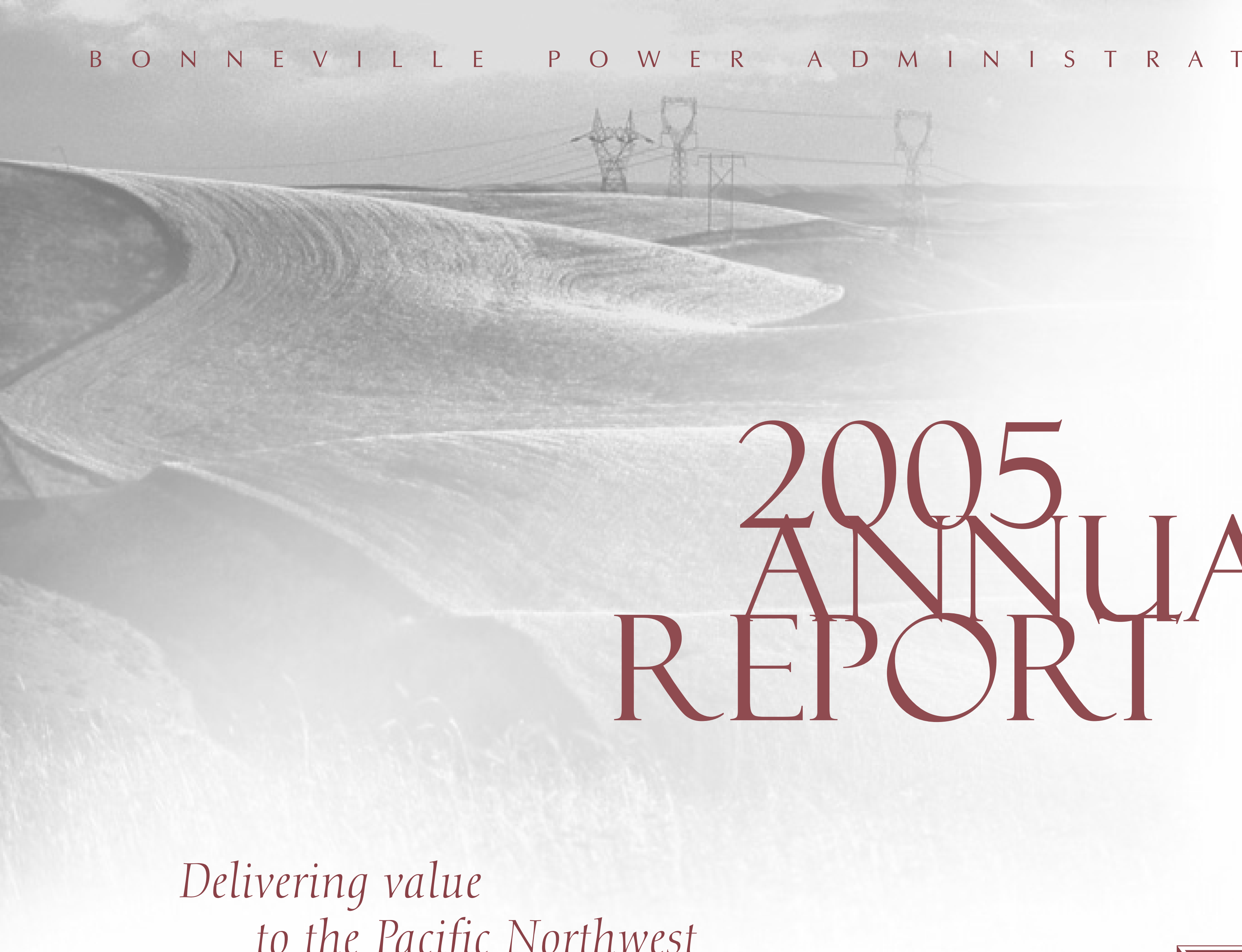


BONNEVILLE POWER ADMINISTRATION

2005 ANNUAL REPORT

Delivering value to the Pacific Northwest

TABLE OF CONTENTS

BPA is proud to be a positive force in the Pacific Northwest. Throughout this report, we've highlighted various ways the agency works to bring value to the region.

DEAR MR. PRESIDENT

Fiscal year 2005 was a year marked by another major stride in improving the Bonneville Power Administration's financial health while making significant investments in our region's electric infrastructure.

We exceeded our revenue targets, earning just over $126 million in modified net revenues, the highest since prior to the West Coast energy crisis. This is our third straight year in the black as we seek to recover from the fallout of the energy crisis.

We opened the year with a decrease in wholesale power rates last Oct. 1. And, we ended the year, on Sept. 30, with another power rate decrease that went into effect the following day. Equally important, we met our obligation to taxpayers by making our U.S. Treasury payment on time and in full for the 22nd year in a row.

I am very proud of these achievements, given the challenges we faced as a power system fueled 90 percent by hydropower. Included in those challenges were our sixth consecutive below-average water year and a court decision that required more costly spill intended to help salmon traverse Columbia and Snake River dams.

It was also a year of major milestones in our business. On the transmission side, we continued our program to shore up the region's reliability, meeting our target for completing construction projects on schedule and within budget. We continued our commitment to help bring renewable power to the region with the interconnection of two wind projects into our transmission system, while another interconnection is scheduled for the end of the calendar year. These projects will help provide energy independence and a buffer against escalating fossil fuel prices. In January, we also achieved a settlement on new transmission rates that went into effect Oct. 1, 2005.

On the power side, we conducted a public process called the Power Function Review to determine program levels for the next power rate period, 2007-2009. We completed a short-term Regional Dialogue to address power sales contract issues pertinent through 2011. As part of this dialogue, we developed policies on service to direct-service industries and on conservation and renewables. We also opened up a long-term Regional Dialogue on BPA's power supply role beyond 2011, when most of our current power sales contracts expire. This process is designed to create more certainty for the region that should lead to more investment in electric infrastructure. We also met our 2005 targets for conservation savings and efficiency improvements to the generating system.

In other areas, we began work on regional standards for resource and transmission adequacy.

Perhaps the most challenging area has been our work in the fish and wildlife arena. The plan that addresses how the federal hydro system is operated for fish listed under the Endangered Species Act has been remanded by a district court, and the federal agencies now have a year to come up with a new plan. But, while that challenge has dominated headlines, we continue to make progress toward achieving biological targets to improve salmon survival.

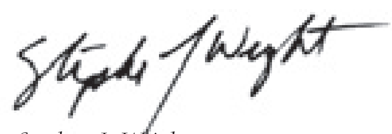
Against the backdrop of these important and sometimes turbulent events, BPA also has been focusing internally. We are in the midst of an agencywide efficiency program designed to further lower costs and maximize our efficiency.

This year we are pleased with improvements in how our customers, constituents and tribes rated our efforts. Composite results from the Transmission, Power and Energy Efficiency customer surveys showed an increase in satisfaction ratings. Constituent scores were also up slightly, while our tribal satisfaction scores were up significantly.

The driving force is our commitment to continue to deliver value to the Pacific Northwest by providing high reliability, low rates consistent with sound business principles, environmental stewardship and accountability. These are the key features Northwest citizens want from their electric power system.

We are an organization committed to public service. The following pages will provide more details on how our agency has performed during fiscal year 2005 to serve the citizens of the Pacific Northwest and meet our responsibilities to the nation's taxpayers.

Sincerely,



Stephen J. Wright
Administrator and CEO

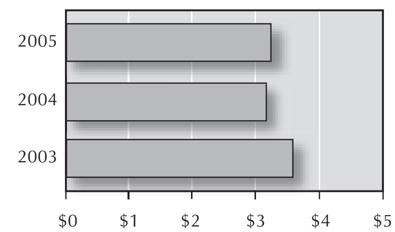
Note: BPA's fiscal year is from Oct. 1 to Sept. 30. Unless otherwise noted, all figures and events in this report refer to fiscal year 2005.

FINANCIAL RESULTS

These charts depict important BPA and Federal Columbia River Power System financial measures. *Net Revenues With and Without Debt Management Actions and Statement of Financial Accounting Standard 133* reflect the impact of nonfederal debt management actions and SFAS 133 (see SFAS 133 and Related Guidance in the first note to the Financial Statements). *Nonfederal Debt Service Coverage Ratio* demonstrates how many times total nonfederal project debt service is covered by net funds available. A ratio of 1.0 is the minimum required to show adequate funds to meet debt service payments to nonfederal bondholders. The *Status of Treasury Principal Repayment* shows the planned and advance payment of federal appropriations and U.S. Treasury bonds. *Financial Reserves* is the sum of BPA cash and deferred borrowing authority at year end.

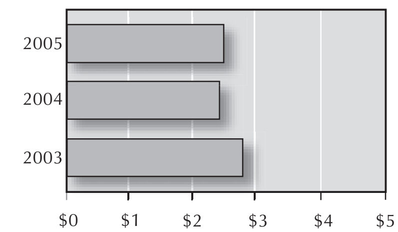
Operating Revenues

billions of dollars



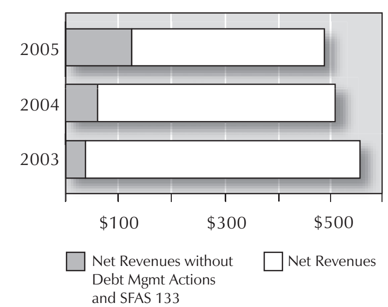
Operating Expenses

billions of dollars



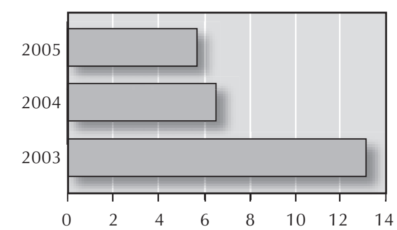
Net Revenues With and Without Debt Management Actions and SFAS 133

millions of dollars



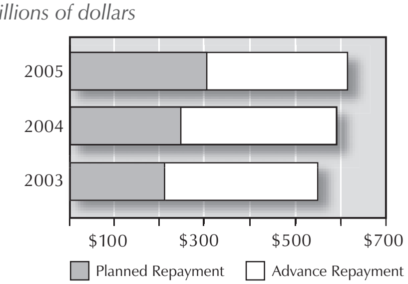
Nonfederal Debt Service Coverage Ratio

times covered



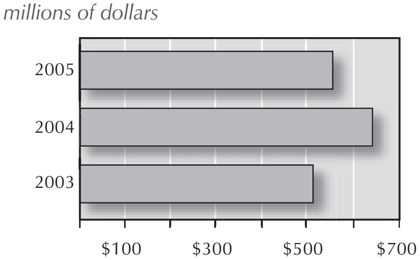
Status of Treasury Principal Repayment

millions of dollars



Financial Reserves

millions of dollars



THE YEAR IN REVIEW

Building Financial Stability

For the first time in five years, we met our modified net revenue targets despite a sixth year of below average water. Aggressive management of our resource portfolio, good market prices, a late wet spell and stringent cost management combined to avert what could have been serious financial setbacks after an extraordinarily dry period in late winter and early spring.

Net revenues for the fiscal year came in at $487 million, compared to $504 million in 2004. Without debt-management actions and the application of SFAS 133,[1] our results would have been $126 million in fiscal year 2005, compared to $66 million in 2004.

For the 22nd year in a row — something we take great pride in — we made our payment to the U.S. Treasury on time and in full on Sept. 30. Our $1.088 billion payment included $616.5 million in principal and $400.7 million in interest. Of the principal, $313 million was a prepayment to retire some Treasury debt early, consistent with our debt optimization program.

BPA maintains a high Treasury payment probability standard as part of our commitment to meeting our responsibilities to U.S. taxpayers for the investment they have made in our system.

Managing FCRPS Debt

Our debt-management policy is aimed at optimizing our Federal Columbia River Power System debt portfolio to keep power and transmission rates low, reduce long-term costs and secure access to capital. Over the last several years, through debt optimization, traditional refinancings and other debt-management initiatives, the weighted average interest rate has decreased from 6.6 percent to 5.6 percent, a savings of more than $100 million in 2005.

Most of the refinancings thus far have been for Energy Northwest nuclear plant debt, although in 2005 BPA and the Eugene Water and Electric Board refinanced older bonds by issuing $26.6 million in refinancing bonds for the now defunct Trojan nuclear plant. The original bonds carried an overall interest rate of 5.9 percent, while the new refinancing bonds carry a rate of 3.3 percent. The result is an annual savings of about $1.5 million through FY 2008.

BPA is extending Energy Northwest debt and using the cash freed up from amortization payments on that debt to

[1] *SFAS 133 refers to Statement of Financial Accounting Standards, Accounting for Derivative Instrument and Hedging Activities.*

retire higher interest outstanding Treasury bonds. As mentioned above, this "debt optimization" has enabled us to repay portions of our obligation to the U.S. Treasury and taxpayers in advance.

Mitigating Risk

The risks the Pacific Northwest faces in its electrical power system are unique. In addition to traditional risks shared by other systems, the Northwest power supply depends on the vagaries of weather since it is a hydro-based system that has limited storage capacity.

We have taken steps to assess risks and to strengthen our ability to respond to and diminish the impact of financial, operational and strategic risks. We have improved policies and reporting analytics for power transactions. Our credit policies have been revamped to allow fair and open access to our transmission assets and to enable sufficient customers to purchase our wholesale power while providing increased protection from customer payment defaults.

The value protected here is significant. We buy and sell to match a highly variable resource to match our customers' loads. Then there are surplus wholesale power sales, made extremely volatile — and therefore risky — by variable hydro generation conditions and unpredictable market prices. Operational risk management concerns range from securing and maintaining necessary workforce skills to litigation expense risks.

Mechanisms to buffer for risk in annual power requirements sales feature prominently in our strategic rate design. In the current (FY 2002-2006) power rate period, BPA is using cost recovery adjustment clauses to ensure cost recovery. While these adjustments allow BPA to keep base power rates lower, rate stability is rarely possible.

Getting More Efficient

If we are to deliver maximum value to the region, we must run our enterprise as efficiently as possible and at the lowest cost consistent with sound business principles. To this end, we are in the midst of a multi-year, agencywide efficiency drive known as the Enterprise Process Improvement Program.

Because of its broad scope, the program is being conducted in increments. To date, implementation of efficiency recommendations is under way in five major internal functions. These include (1) information technology; (2) transmission plan, design and build; (3) public affairs; (4) human resources, and (5) energy efficiency contract administration.

Work is currently under way to review systems and processes in four additional functions, including (1) marketing and sales, (2) asset management, (3) supply chain, and (4) transmission operations and maintenance.

As we conduct the efficiency initiatives, we are taking care that organizational changes meet Standards of Conduct approved by the Federal Energy Regulatory Commission.

The efficiency program has already led to consolidation and centralization of some agency functions, elimination of redundancies and establishment of consistent processes to ensure approaches can be replicated in the future. The latter is important because a significant portion of BPA's work force is eligible to

KEEPING THE LIGHTS ON

BPA replaced tower parts near the summit of Wyoming's Teton Pass with components designed to better withstand the area's icy weather. The work will reduce outages and shore up the reliability for the Jackson Hole area. It is just one of several recent transmission projects that have included new construction, rebuilds and upgrades to increase system reliability.

retire over the next three-to-five years. BPA will use these retirements and other separations as an opportunity to meet downsizing goals.

Keeping Rates Low

FY 2006 power rates

At the beginning of this fiscal year, BPA implemented a 7.5 percent reduction in its wholesale power rates. A year later, BPA announced it would begin the 2006 fiscal year with a 1.6 percent reduction despite severe challenges. The drop in the fiscal year 2006 rate was possible because of a very strong wholesale power market and expense reductions that offset some of the effects of dry weather and the costs of additional court-ordered operations for listed salmon. The higher prices in wholesale power supply markets are the result of short supplies in the Western U.S. market and high natural gas prices, which tend to drive wholesale electricity prices.

FY 2007-2009 power rates

FY 2006 is the final year of the current five-year power rate period (FY 2002-2006). In preparation for setting rates for fiscal years 2007-2009, BPA conducted a Power Function Review, a public process that gave the region the opportunity to examine and provide input on the cost projections that formed the basis for BPA's Initial Rate Proposal. The Power Function Review helped BPA identify reductions in projected costs totaling $96 million a year for the FY 2007-2009 period, and we are continuing to explore further cost reductions.

Direct-service industries

BPA has a longstanding relationship with large aluminum companies that have been served directly by BPA. While we do not have a legal obligation to serve these direct-service industries after current contracts expire in FY 2006, we have established a framework for service in the 2007-2009 power rate period. This framework provides a known and capped cost and is designed to balance the industries' ability to sustain and create jobs against the need to minimize rate impacts to other customers. The benefits proposed for the aluminum smelter DSIs were set at 577 average megawatts with a cost cap of $59 million per year. These allocations are higher than the current operating levels for all of the smelters.

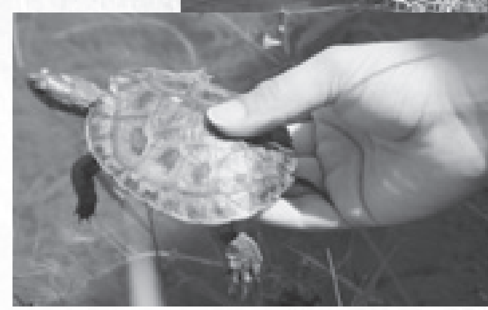
Transmission rates

In January, BPA reached a settlement agreement with customers for a 12.5 percent increase for transmission rates beginning Oct. 1, 2005, for a two-year rate period. This represents an increase of between 1 and 2 percent of a customer's total delivered wholesale power cost. Actual rate increases vary depending on what type of transmission service customers purchase.

The primary driver of the increase was a shortfall in transmission sales and revenues as well as costs associated with major infrastructure projects to improve system reliability. There has been a more than 3,000-megawatt drop in network transmission sales since 2001 due to losses of regional load (especially the direct-service industries) and due to customers finding more efficient ways to use their existing firm transmission rights.

Prior to setting rates, our Transmission Business Line conducted a public process to solicit input on planned capital and expense levels. In response to public comments, TBL reduced its forecast capital program by over

Fifty-two Western pond turtles were re-released into the wild thanks to a partnership between BPA and the Oregon Zoo. The turtles spent nine months at the zoo growing large enough to avoid being eaten by non-native predators such as bullfrogs and largemouth bass. Just a year ago, the turtles were on the verge of extinction in Washington state with only 150 left in the wild. Today, their numbers have climbed to nearly 1,000.



HELPING ENDANGERED SPECIES

$122 million from the initial proposal for fiscal years 2006-2007.

Building Reliable Transmission

BPA met its targets to keep unplanned system outage frequencies and duration for key circuits within stringent control limits. Our system had no involuntary curtailments related to security breaches or cascading failures.

BPA has targeted its transmission investments in those congested areas that have the highest need for additional capacity. Since 2001, we have invested over $1 billion in transmission system projects that include construction of new high-voltage lines, rebuilding existing lines and substation upgrades.

A major milestone for fiscal year 2005 was energization of the 84-mile Grand Coulee-Bell 500-kilovolt line in eastern Washington last December. This was our largest transmission project in two decades and one of the largest in the nation. It relieves congestion in the flow of power from east to west and maintains system reliability while increasing capacity to move cost-effective generation to consumers.

During the year, BPA also:

- Completed the 115-kV Franklin-Walla Walla project in Washington state;
- Energized the115-kV Raymond-Cosmopolis rebuild project in southwest Washington;
- Energized the 115-kV Anderson Ranch-Mountain Home rebuild in Idaho;
- Upgraded a 115-kV line between Albany-Eugene in Oregon to enhance service to industrial loads;
- Continued construction on the 161-kV Swan Valley-Goshen rebuild in Idaho;
- Scheduled energization of the 500-kV Schultz-Wautoma line in central Washington for November 2005; and
- Rebuilt towers on the Swan Valley-Teton 115-kilovolt lines in Wyoming to solve winter icing problems.

TBL put a hold on proposed construction of a new 500-kV line from McNary Dam to John Day Dam along the Columbia River after we did not receive sufficient commitments from potential users to help fund construction. The line would facilitate integration of new power plants onto the grid but is not needed for system reliability.

In other transmission developments, we completed revision of our Available Transmission Capability methodology following a two-month public process. The changes were directed at refining modeling assumptions to more accurately project physical flows of electrons over network flowgates under peak loading conditions. This will allow increased availability of firm service.

BPA also signed General Transfer Agreements with over 80 primarily rural utilities that receive power from BPA over transmission lines owned by other utilities. The agreements assure the utilities that they will continue to receive adequate transmission service over the next 20 years at rates equivalent to customers served directly through BPA lines even if some form of a regional transmission organization is put in place.

Seeking Non-wires Solutions

A BPA-sponsored Non-Wires Round Table made up of industry, utility and environmental members has been working to make non-wires solutions viable to the Northwest. Such solutions

Providing Reliable Power

The 84-mile Grand Coulee-Bell 500-kilovolt line in eastern Washington was completed ahead of schedule and under budget. It is one of the largest transmission lines built in the nation in the last 20 years. The line relieves congestion from east to west and enhances system reliability while increasing capacity to move cost-effective generation to consumers. BPA has one of the biggest transmission infrastructure building programs in the nation.

won't eliminate the need for new transmission lines but can reduce and defer the need. Non-wires solutions include demand reduction, direct load control, distributed generation and enhanced energy efficiency.

As part of this effort, this past year we began funding a pilot project that would allow utilities to directly control irrigation pump motors during periods of heavy electricity use. We hope to test 400 pumps in the next two years. If it proves out, the utilities should be able to curtail 5 megawatts (enough power to serve 3,000 homes) for one hour.

We also are working with three public utilities to test direct load control technology in the Olympic Peninsula. Under the project, load control devices will be installed on water heaters and heating and cooling systems in 2,500 homes. At times of peak demand, utilities would page the controllers, which would reduce use of the appliances as needed. BPA expects to have 5 megawatts of curtailable load when all units are installed.

Investing in Generation

The Federal Columbia River Power System includes 31 operating federal hydroelectric projects with over 200 generating units. Through direct funding and the close cooperation of the U.S. Army Corps of Engineers and Bureau of Reclamation, BPA uses its borrowing authority from the U.S. Treasury to make investments needed to restore generation availability and improve efficiency, eliminating demand on Corps and Reclamation annual appropriations for power-related investments. During fiscal year 2005, enhancements to the system increased system efficiency by 20 megawatts.

The system hydro generating units also met their reliability targets for availability in heavy-load hours, and there were no involuntary curtailments of firm load as a result of inadequate power supply or security breaches. The Northwest Power and Conservation Council and BPA's internal analysis both indicate regional and federal power supply will be sufficient through the coming fiscal year.

Since the beginning of the direct funding arrangement, BPA has improved system performance. However, given that the hydro system continues to age and represents critical resources needed to meet our obligations, we will need to continue to invest in the hydroelectric projects. Since direct funding began, BPA has invested approximately $560 million in generation reliability and efficiency enhancements. We have budgeted $1 billion over the next

12-15 years to continue to preserve and maintain the existing generation facilities. Without these investments, we expect hydropower availability would decline at a rate of about 1.5 percent per year initially and could go higher as the equipment ages further. Similarly, moving forward with cost-effective opportunities to expand the existing federal generation system through efficiency improvements is a smart economic and environmental decision when compared to purchasing power from the market.

Promoting Energy Efficiency

Long-term investments in energy efficiency help buffer the region against future resource uncertainties. During periods of price volatility, conservation also helps reduce financial risk associated with relying on the market for energy purchases.

Increasing Efficiency

Enhancements to the hydro system during the year increased system efficiency by 20 megawatts. Moving forward on cost-effective opportunities to expand the existing federal generation system through efficiency improvements makes economic sense when compared to purchasing power from the market.

From 1982 through 2004, BPA's conservation and efficiency efforts have netted 850 megawatts of savings for the region, comparable to the output of two coal plants. In addition to direct programs, BPA has promoted energy-efficient building codes and supported the purchase of more energy-efficient appliances.

In fiscal year 2005, we exceeded our target of 40 megawatts of new conservation by capturing 43 megawatts in the load we serve. Our Federal Agency Energy Efficiency Program also surpassed the year's target for efficiency savings while remaining the lowest cost conservation acquisition program. BPA realizes proportionately more savings from the federal sector than any other sector in the regional economy.

During the year, BPA initiated a study of irrigation scheduling actions, sponsored programs for remote control of power equipment, offered a rebate program for more efficient irrigation equipment and conducted a buy-down of compact fluorescent lamps.

BPA also committed $10 million for each of the next five years to fund work of the Northwest Energy Efficiency Alliance. The Alliance supports market-based energy efficiency programs in the region.

BPA also continued its support of weatherization of low-income Native American homes. This year, 76 homes were weatherized, bringing the total to 160 homes.

A highlight of the year was receiving a Star of Energy Efficiency award from the Alliance to Save Energy. The Natural Resources Defense Council nominated BPA in recognition of our work on non-wires alternatives to transmission as well as successful promotion of conservation as a cost-effective resource for the Northwest.

Facilitating Renewable Energy

BPA purchases power from six wind projects with a total 198-megawatt capacity, which represents 37 percent of the region's current wind capacity of 537 megawatts. Our evolving role in the region makes it very unlikely that we will be a substantial buyer of wind (or any other resource) in the future. Instead, BPA is transitioning to a role as a facilitator of new, customer-owned renewable projects by providing ancillary services for wind projects.

BPA also plays an important role in providing the infrastructure to deliver power from new and existing wind projects. At this time, more than 300 megawatts of combined peak output are connected to the BPA grid.

PROMOTING RENEWABLES RESOURCES

This year, BPA completed interconnections for two more wind projects, which are now operating. A third interconnection will be completed by the end of the calendar year, with wind production scheduled to begin in early 2006. We are working on 10 other requests from wind developers that plan to interconnect to the system by 2007.

BPA also began development of a new “conditional firm” transmission product that would allow long-term firm transmission capacity to be sold with the proviso that service could be curtailed during some parts of the year. This could allow use of presently underused capacity on critical transmission pathways. At the same time, it would give wind generators better access to transmission grids. Development of the product is currently “on hold,” as our Transmission Business Line focuses on putting in place the scheduling and

BPA interconnected 75 megawatts of new wind power from the Klondike II wind farm just outside of Wasco, Ore. It is the sixth wind interconnection into BPA’s transmission system, which now includes over 300 megawatts of combined peak output. Ten other requests for interconnection are in the queue.

curtailment systems needed to implement the conditional firm product.

BPA expects to maintain its renewable energy program level at up to $21 million net expense annually. The renewable program also realizes some revenue through sales of environmentally preferred power.

And, BPA is practicing what it preaches. The agency increased its purchase of green power from PacifiCorp this past year so that 12 percent of the energy for our headquarters building now comes from renewable wind power.

Planning for the Future

With existing power contracts due to expire in 2011, BPA must establish its future power supply role. As part of our commitment to promote regional electric infrastructure development, we are working toward new 20-year power sales contracts. We initiated this process now to give our customers adequate time to understand their obligation to take future actions to develop resources. We believe increased clarity about how much power BPA will provide for load placed on us beyond 2011, and at what price, is essential to assuring adequate infrastructure.

In August, we released a "concept paper" designed to facilitate discussion and bring some closure on outstanding issues that need to be settled to define BPA's long-term power supply role. The concept paper is not a decision document, but rather a collection of broad proposals intended to stimulate discussion and bring about alignment.

A key concept is to limit the amount of power sold at the lowest cost to the output of the federal system; this power would be sold under Tier 1 rates. Customers would bear any additional costs (Tier 2 rates) if BPA has to develop or purchase resources to meet loads beyond the federal system resources.

Our goal is to offer new long-term contracts by April 2007 and complete the long-term tiered rate methodology to accompany new contracts by October 2008. Before contracts can be signed, a number of major policy decisions must be made. These decisions include:

- Service to public utilities
- Exchange benefits
- Service to direct-service industries
- Resource adequacy standards
- Cost controls and dispute resolution
- Conservation and renewables

Protecting Fish And Wildlife

BPA funds a diverse and comprehensive fish and wildlife program to address impacts of federal hydropower development on Columbia Basin fish and wildlife. The program is guided by the Northwest Power and Conservation Council, NOAA Fisheries[2] and the U.S. Fish and Wildlife Service. The latter two agencies administer recovery programs for fish and wildlife listed under the Endangered Species Act.

The federal agencies' effort to protect endangered salmon and steelhead in the Columbia Basin has been built on a carefully coordinated set of measures involving hydro operations, hatcheries, habitat and harvest management. Individually, no measure is a so-called silver bullet, but, taken collectively, these coordinated measures are producing results.

This year, new efforts included improvements in dam and flow configurations and installation of a removable

A removable spillway weir, often called a fish slide, was installed at Ice Harbor Dam on the Snake River where it is helping juvenile fish migrate past the dam. The slide gives smolts an easier and safer ride because it passes spill close to the water surface, giving fish a slower, low-pressure ride. At the same time, it also uses less water to do the job, thus saving ratepayer dollars.

HELPING SALMON SURVIVE

[2] *NOAA Fisheries, headquartered in Seattle, Wash., is a regional division of the National Marine Fisheries Service, which is part of the U.S. Department of Commerce.*

spillway weir, sometimes referred to as a fish slide. Removable spillway weirs have been tested and installed at some Snake River dams, while others are planned for the future in both the Snake and Columbia rivers. These fish slides not only improve fish passage for juvenile fish migrating downstream, but do so using less water, thus making them more cost effective.

In addition, efforts on behalf of both anadromous and resident fish addressed protection and restoration of critical spawning and rearing habitat, water leases, enhanced control of salmon predators and improvements in hatchery and harvest management. BPA also funded or helped fund purchase of 20,000 acres of land and easements for wildlife habitat in 2005.

All together, the federal investment in fish and wildlife amounts to over $500 million annually. Because there is so much at stake, BPA continues efforts to move beyond measuring the success of fish and wildlife programs by how much we spend. We are working with other regional parties to define biological objectives — such as survival rates — then pursue the most cost-effective ways to achieve those biological objectives. We also are pursuing program reinvention to put more of the available funds "on the ground" where they will most directly benefit fish and wildlife. This includes exploring cost-sharing opportunities and working with the Council as it develops a new program framework for research, monitoring and evaluation.

BPA, the U.S. Army Corps of Engineers and Bureau of Reclamation are continuing to monitor performance and provide results in annual progress reports. Comprehensive performance evaluations are due in 2007 and 2010.

Biological opinion litigation

Litigation, dating back to 1995, continues over operation of the Federal Columbia River Power System. With input from the federal action agencies (BPA, the Corps and Reclamation), NOAA Fisheries had issued biological opinions that address how the federal hydro system would be run to protect and rebuild 12 salmon runs listed under the Endangered Species Act. The National Wildlife Federation and other parties challenged the 2000 Biological Opinion, then subsequently a new 2004 Biological Opinion, contending that protections for threatened and endangered salmon are inadequate.

In May, District Court Judge James Redden issued an opinion finding the

2004 FCRPS Biological Opinion inconsistent with the requirements of the Endangered Species Act. In a separate June 10 action, the court granted the plaintiffs' request for additional spill at four federal dams on the Columbia and Snake rivers. This order applied only to spill during the summer of 2005. The cost of the lost energy value to the region was about $74 million for the additional spill.

In early October 2005, Judge Redden ordered NOAA Fisheries to develop a new plan for operating the federal hydro system and set a deadline of one year. The new plan would be the subject of a new biological opinion and would be integrated with other long-term salmon recovery efforts already under way. However, the plaintiffs are currently seeking what could be costly changes in hydro operations before the new biological opinion is in place.

BPA continued support for weatherization of low-income tribal housing. During the year, 76 Native American homes were weatherized. Contracts for work also were awarded to three Indian-owned and operated business. BPA's work with the tribes includes protection of cultural resources, agreements on transmission easements and protection of fish and wildlife.

WORKING WITH THE TRIBES

Fostering Innovation

This year BPA established a new Office of Technological Innovation to lead development and management of the agency's strategy for research, development, demonstration and deployment of new technology. The office will focus primarily on adapting those technologies that have already been successfully researched and developed for demonstration programs and commercial deployment in the region. BPA sees this effort as one more way to bring value to Northwest citizens.

The BPA Wind Forecasting Network went into full operation in June. The two-year research and demonstration project will work to forecast wind generation at operating wind plants from real time to several days in the future. We believe it is the first effort of its kind in the U.S.

BPA worked with the Department of Energy and Energy Northwest to run a pilot project to turn depleted uranium materials into new fuel for the Columbia Generating Station nuclear plant. If successful, the project could produce eight years of fuel at a savings of about $80 million.

BPA also is working with the Idaho National Lab on new security technology such as unmanned aerial vehicles for line patrol and transmission and tower sensors to monitor barrier technology.

Enhancing Grid Reliability

The Northwest grid currently is managed by 17 individual control area operators serving more than 20 generating and transmitting utilities. BPA believes the Northwest needs an effective one-utility approach to assure high reliability and increase efficiency in the future.

BPA has been working with regional parties for nearly a decade on approaches to restructure transmission service to address the region's transmission needs. Throughout fiscal year 2005, the region worked on two parallel approaches, Grid West and the Transmission Improvements Group, known as TIG. BPA provided funding for development of both and conducted a public process in August to invite further regional discussion on these alternatives.

Grid West proposed a new independent entity under Federal Energy Regulatory Commission jurisdiction that would be an independent transmission provider with some features of regional transmission organizations in other parts of the country. However, it would be significantly scaled back to reflect Northwest needs and interests.

The TIG approach proposed a set of contracts among utilities to provide many, but not all of the functions of Grid West. These contracts would be administered under the overall coordination of a small staff and board, also created by contract. The TIG approach would not fall under FERC jurisdiction.

The TIG and Grid West proposals had much in common, but they also reflected key differences in the interests and perspectives of various institutions in the region today. As a result, BPA asked the region to explore a strategy to integrate the best of both proposals.

However, Grid West declined the integration proposal shortly after the end of the fiscal year and decided to pursue its original proposal. BPA

INVESTING IN OUR YOUTH

Academic stars got to shine as over 80 schools in Oregon and western Washington participated in the BPA-hosted regional Science Bowls for junior high and high school students. Nearly 100 employees and their families volunteered to help in the event.

resigned from the Grid West Board after the board limited membership to entities that fund work toward its design for a regional transmission entity.

While agreement in the region remains elusive, BPA continues to believe that a plan that combines the features of the two competing proposals is sound and responsible, and we continue to work toward that end. We also believe that continuing separate operations or a fragmented approach is not in the best interests of the region.

Ensuring Adequacy

While BPA is investing in infrastructure on its own system and will capture all cost-effective conservation within its own load, we cannot support the entire regional infrastructure. The region needs to take an integrated approach in key areas such as resource acquisition and transmission infrastructure. We believe regional resource and transmission adequacy standards are critical to defining responsibility and accountability and to weighing the value of different investments.

Transmission adequacy

BPA is participating in a regional effort hosted by the Northwest Power Pool to develop transmission adequacy guidelines. This effort would complement existing reliability criteria provided by the North American Electric Reliability Council and Western Electricity Coordinating Council. Once the guidelines are approved, regional utilities will decide whether to adopt and voluntarily comply with these guidelines. The proposed timeline to address the first set of issues is January 2006. The process involves developing a framework and identifying potential ways to measure transmission adequacy. The first set of draft guidelines is expected to be available for public comment by the end of the calendar year. We will go through the appropriate National Environmental Policy Act process and will host a public comment period before making any decisions.

Resource adequacy

BPA is working with regional parties and the Northwest Power and Conservation Council to develop a standard/framework that assures the region will have adequate generating resources in place to reliably serve load without high and volatile costs. This is important because the region has said that it does not want BPA acquiring new resources and it wants BPA to limit sales of its lowest price power to the Federal Base System.

There is significant support for developing a regional resource adequacy metric and target, which taken together constitute such a standard. However, views on mechanisms to implement a resource adequacy standard vary widely.

A technical committee is being tasked with developing common load forecasting, resource counting and delivery protocols and with providing options for metrics and targets to assess adequacy at the regional levels. A policy-level steering committee will then select appropriate metrics and targets that constitute a regional resource adequacy standard. The committee will decide whether such a standard should be translated to the utility-specific level and will explore ways to implement such a standard. The steering committee expects to complete its decision-making process by late spring of 2006. This effort is intended to be compatible with Western Electricity Coordinating Council and North American Electric Reliability Council resource adequacy efforts.

FOSTERING ENERGY EFFICIENCY

BPA promotes efficiency in all sectors – residential, commercial, industrial, agricultural and government. In the agricultural sector, BPA tested irrigation pumps to identify efficiency opportunities and provided rebates for high-performance, low-pressure sprinklers. There's also a pilot effort to capture energy savings associated with irrigation scheduling. This year, BPA exceeded its targets for capturing conservation savings across all sectors.

Keeping the System Secure

BPA implemented Operations Security and Continuity of Operations programs in all BPA organizations this past year, with substantially all employees completing online security and cyber security training. We completed security enhancement projects at our headquarters, Celilo and Ross facilities and provided guidance for security systems at 17 BPA substations. Buffer zone protection plans for critical facilities were completed in cooperation with regional law enforcement agencies and the Department of Homeland Security.

We signed a unique contract with Washington state's King County to fund security systems for three critical BPA facilities located within the county. BPA also helped establish the new Western Energy Coordinating Council physical security work group and successfully participated in the recent WECC compliance review.

Working in the Community

Involvement with local communities is important to BPA, and we are involved both as an agency and through our employees. On the more global community level, BPA delivered six large portable generators to the Oregon National Guard for delivery to Louisiana. The generators were sent to power health facilities in the area devastated by Hurricane Katrina. At the Department of Energy's invitation, our vice president for Engineering and Technical Services traveled to Texas to help restore power for Hurricane Rita victims. We are standing by to help in other ways as the area rebuilds its infrastructure.

In May BPA received an award from the Department of Energy for having the highest participation in the DOE Community Service program. A number of employees also received Utility Partnership Volunteers Awards from the U.S. Energy Association for their volunteer work helping developing countries set up their electricity infrastructure.

Major community events we sponsor or co-sponsor include the Science Bowl, local and state science fairs, community festivals, school-to-work programs and Earth Day events. We also co-sponsor educational programs such as the Hydromania Summer Science Camp for children in low-income areas and the Kids in the Creek program.

In Vancouver, Wash., where our Transmission center is located, we donated land to help the city expand its greenway trail system, helped facilitate a bike/running path in a transmission corridor and — in an extremely popular move — opened nine acres on our Vancouver Ross Complex grounds to be used as an off-leash dog recreation area.

Last fall, we worked with several Northwest tribes, the U.S. Army Corps of Engineers and Washington State Parks to set up a display of 43 Native American petroglyphs and pictographs in a place befitting their importance to tribal culture. BPA has provided many thousands of acres of habitat for fish and wildlife, and last October we partnered with the Nature Conservancy on the Willow Creek Wildlife Mitigation Project in Oregon's Willamette Valley. The land not only will protect fish and wildlife, but endangered plants as well.

HELPING THOSE IN NEED

The Oregon Air National guard delivered six 30-kilowatt portable generators, each weighing a ton, to hurricane-ravaged Louisiana. The BPA generators were used to power health facilities in areas where the electricity infrastructure had been destroyed.

Recognizing Employees

As of mid-August 2005, our employees numbered 3,028, down 5 percent since 2002. We had a number of changes in our executive staff this year due to retirements. This trend reflects the fact that 19 percent of our current work force will be eligible to retire by the end of fiscal year 2006. This has put our efforts to ensure succession planning into sharp focus. The Enterprise Process Improvement Program currently under way is emphasizing standardizing and recording processes so that key functions will run efficiently as experienced staff retire and new employees move in.

In May, we introduced a new employee innovation program called Making ene. In just the first four months, employees submitted 58 innovations compared to 39 new ideas for the entire fiscal year 2004. Many ideas focused on cost savings, which is an ongoing theme at BPA.

Our annual Employee Survey response was over 74 percent, up about 11 percent from the past several years. The overall score was down only 1 percent despite the major efficiency changes taking place throughout the agency that have included consolidation, physical moves, staffing changes and restructured functions. This speaks well for the resiliency of our employees and of their support for building a more efficient organization so that we can provide better value to the Pacific Northwest.

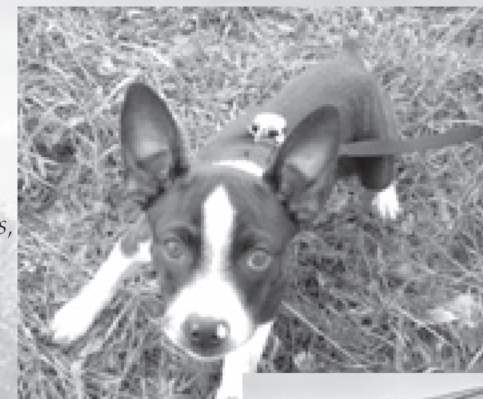
And Looking Forward

A hallmark of 2005 has been a focus on the future. It was the first full year under a new long-term strategic direction set the year before. And, it proved its worth in setting direction and focusing us on the long term. The Regional Dialogue on BPA's future power supply role, along with infrastructure development, risk management, technological innovation, conservation and renewables, adequacy standards and efficiency initiatives — all speak to setting the stage for the region's long-term energy future.

This is a pivotal time for the Pacific Northwest. The region faces significant decisions over how to meet future energy needs. There is a fair degree of agreement in the region today around broad goals, but much work needs to be done in implementation details. We believe that by engaging the region in the important issues covered in this report and encouraging our multiple constituencies to come to the table prepared to seek consensus, we can help the region build an energy future that is stable, reliable, low cost and environmentally friendly. This is the future that will make and keep the region's economy and its environment healthy.

PARTNERING IN THE COMMUNITY

Dog owners, along with their best friends, cheered when BPA donated use of nine acres at the south end of its Ross Complex in Vancouver, Wash., as an off-leash dog recreational area. A nonprofit group of dog owners put up fences, installed waste disposal stations and will maintain the area for the community.



PERFORMANCE MEASURES

Each year since 1996, BPA has selected a set of measurable targets that the agency as a whole is responsible for achieving. These act as indicators of overall agency performance and are used in evaluating agency management. In fiscal year 2005, BPA was in the successful range for 16 of 18 targets.

Target met

Critical infrastructure milestones

We met critical milestones for 11 key projects in an expansive transmission infrastructure building program, possibly the biggest such program in the country. Capital expenditures were well within the goal of not exceeding $108 million. BPA met its target to increase hydro system generating efficiency by 20 average megawatts.

Target met

Conservation

BPA achieved 43 average megawatts of new conservation exceeding its target for the year of 40 average megawatts. New conservation augmentation was obtained at a cost of under $1.0 million per average megawatt and below the target range of $1.2 million to $1.4 million.

Target met

Transmission reliability

BPA succeeded in all three portions of this target. Unplanned outage frequency and duration on key circuits were within established limits, there were no involuntary curtailments of firm load due to transmission system security breach, and there were no cascading failures.

Target met

Generation reliability

Heavy load hour availability for the year was 100 percent, and there were no generation-related involuntary curtailments of firm load.

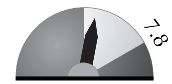
Target met

Regional Dialogue

We kept to our schedule on the Regional Dialogue process and engaged the region in important discussions about our future power supply role.

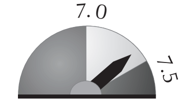
Customer, constituent and tribal satisfaction

Customer
7.2



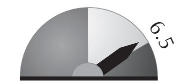
Target met

Constituent
7.0



Target met

Tribal
5.5



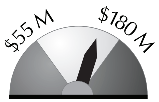
Target met

BPA was in the successful range for all three of these targets, scoring 7.3 for customer satisfaction; 7.4 for constituent satisfaction; and 6.4 for tribal satisfaction.

Target met

Internal operating costs

Overall expenditures (including capital and expense) were $452 million for the year, representing 90 percent of the start-of-year budget.



Target met

Modified net revenue

For the first time in five years, we met our modified net revenue target achieving $126 million. The target was $55 million to $180 million. Part of this result was due to better than expected market prices, but a significant part was due to great staff work and a united, agencywide effort to be as efficient as possible.

Target met

Rate levels

We reduced power rates for the third year in a row, and kept our transmission rate increase below the targeted level.

Target met

Treasury payment

BPA made its payment of $1.088 billion to the U.S. Treasury in full and on time.

Target met

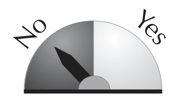
Sustainable access to capital

BPA established a capital management strategy that is sustainable through 2018 and can adapt to contingencies through 2011. BPA met all elements of the target when the $313 million accelerated payment to the Treasury was made at year end.

Target met

Biological opinion

We worked with other federal agencies to produce a new biological opinion. Although it was rejected by the district court, BPA believes it is superior to the previous opinion and provides greater benefits for listed fish.



Target not met

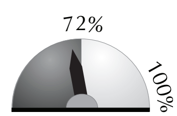
Biological opinion litigation

We did not meet our target to achieve an outcome on biological opinion litigation that is consistent with our financial objectives, and that continues to be a contentious issue.

Target met

System and process improvement

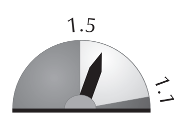
BPA completed five of six major process redesigns and approved these for implementation. Additional reviews will be conducted in FY 2006.



Target not met

Employee understanding of BPA business strategy

Based on an annual survey, 70 percent of employees confirmed that they understood BPA's business strategy, just missing the target of 72 percent.



Target met

Safety

BPA's annual accident frequency rate was 1.4, within the target range of 1.1 to 1.5 and 41 percent lower than the utility industry average of 2.4. There were no fatal injuries.

Petroglyphs (rock carvings) and pictographs (rock paintings) were given a site worthy of their status as sacred objects to Northwest Indians. BPA helped fund and facilitate their move to a state park on the Washington side of the Columbia River. The items had been taken from an area later inundated by the reservoir behind The Dalles Dam.

PRESERVING NORTHWEST CULTURE

FINANCIAL SECTION

MANAGEMENT'S DISCUSSION & ANALYSIS

General

The Federal Columbia River Power System (FCRPS) combines the accounts of the Bonneville Power Administration (BPA), the accounts of generating facilities of the U.S. Army Corps of Engineers (Corps) and the Bureau of Reclamation (Reclamation) and the operation and maintenance costs of the U.S. Fish and Wildlife Service (Fish and Wildlife) for the Lower Snake River Compensation Plan Facilities.

BPA was created by an act of Congress in 1937 to market electric power from the Bonneville Dam located on the Columbia River and to construct facilities needed to transmit the power. Congress has since designated BPA to be the marketing agent for power from all of the federally owned hydroelectric projects in the Pacific Northwest. BPA, headquartered in Portland, Ore., is one of four regional federal power marketing administrations within the U.S. Department of Energy. Many of BPA's statutory authorities are vested in the Secretary of Energy, who appoints, and acts by and through, the BPA administrator. Some other authorities are vested directly in the BPA administrator.

BPA's primary enabling legislation includes the following federal statutes: the BPA Project Act of 1937; the Flood Control Act of 1944; the Regional Preference Act (Public Law 88-552); the Federal Columbia River Transmission System Act of 1974; and the Northwest Electric Power Planning and Conservation Act of 1980 (Northwest Power Act). BPA now markets electric power from 31 federal hydroelectric projects, most of which are located in the Columbia River Basin and all of which are owned and operated either by the Corps or Reclamation. These projects have an expected aggregate output of roughly 9,000 average megawatts under median water conditions. BPA has acquired all of the generating capability of Energy Northwest's Columbia Generating Station (CGS) nuclear power plant. The contract to acquire the generating capability of the project, referred to as a net-billing agreement, requires BPA to pay all or part of the annual project budget, including operating expense and debt service. BPA also acquired all of the output of the Cowlitz Falls hydro project and agreed to pay the operating expense and debt service. BPA sells, purchases and exchanges firm power, non-firm energy, peaking capacity and related power services. BPA also constructed and operates and maintains a high-voltage transmission system comprising approximately three-fourths of the bulk transmission capacity in the Pacific Northwest. BPA uses this transmission capacity to deliver power to its customers and makes transmission capacity available to other utilities and power marketers.

BPA's primary customer service area is the Pacific Northwest region of the United States, encompassing Idaho, Oregon, Washington, parts of western Montana, and small parts of western Wyoming, northern Nevada and northern California. BPA estimates that the population of the 300,000 square-mile service area is approximately 11 million. Electric power sold by BPA accounts for about 40 percent of the electric power consumed within the region. BPA markets the majority of this power to over 100 publicly owned and cooperatively owned utilities for resale to consumers in the region. BPA also has contracts to sell power for direct consumption to a small number of companies (direct-service industries or DSIs) located in the region, although the contracted amount of service BPA provides to DSIs has diminished substantially relative to levels from the 1940s through the 1990s. BPA is also required by law to exchange power with qualifying utilities to meet their residential and small-farm electric power loads within the region. The operation of this program, referred to as the Residential Exchange Program, may result in payments by BPA to the exchanging utilities if the applicable power rates for FCRPS power are lower than the utilities' respective average system cost of meeting their residential and small-farm power loads. The primary participants in the Residential Exchange Program historically have been investor-owned utilities in the region.

The Transmission System Act placed BPA on a self-financing basis, meaning that BPA pays its costs from revenues it receives from the sale of power and the provision of transmission and other services, which BPA provides at rates that seek to produce revenues that recover BPA's costs, including certain payments to the U.S. Treasury. BPA's rates for the foregoing services are subject to approval by the Federal Energy Regulatory Commission (FERC) on the basis that, among other things, they recover BPA's costs. BPA issues and sells bonds to the U.S. Treasury and uses the proceeds thereof to fund certain activities established under federal law.

With the Energy Policy Act of 1992, BPA was required to provide open access, non-discriminatory transmission service to all requestors using pro forma tariffs as approved by FERC. After certain national regulatory initiatives to promote competition in wholesale power markets were announced, BPA separated its power marketing function from its transmission system operation and electric system reliability functions in 1996. While BPA is a single legal entity, it conducts its business as separate business lines — the Power Business Line (PBL) and the Transmission Business Line (TBL).

BPA's cash receipts from all sources, including from both its transmission and power marketing business lines, must be deposited in the BPA fund, which is a revolving fund account of the U.S. Treasury and which is available to pay BPA's costs. In accordance with the Transmission System Act, expenditures made by BPA from the BPA fund "shall have been included in annual budgets submitted to Congress, without further appropriation and without fiscal year limitation, but within such specific directives or limitations as may be included in appropriation acts, for any purpose necessary or appropriate to carry out the duties imposed upon [BPA] pursuant to law."

BPA is required to make certain annual payments to the U.S. Treasury. These payments are subject to the availability of net proceeds, which are gross cash receipts remaining in the BPA fund after deducting all of the costs paid by BPA to operate and maintain the FCRPS other than those used to make payments to the U.S. Treasury for: the repayment of the federal investment in certain transmission facilities and the power generating facilities at federally owned hydroelectric projects in the Pacific Northwest; debt service on bonds issued by BPA and sold to the U.S. Treasury; repayments of appropriated amounts to the Corps and Reclamation for certain costs allocated to power generation at federally owned hydroelectric projects in the Pacific Northwest; and costs allocated to irrigation projects as are required by law to be recovered from power sales. BPA met its fiscal year 2005 payment responsibility to the U.S. Treasury of $1.088 billion in full and on time. BPA has made all payments to the U.S. Treasury in full and on time since 1984.

The requirement to pay the U.S. Treasury exclusively from net proceeds would result in a deferral of U.S. Treasury payments if net proceeds were not sufficient for BPA to make its payments in full to the U.S. Treasury. Such deferrals could occur in the event that BPA were to receive less revenue or if BPA's costs were higher than expected. Such deferred amounts, plus interest, must be paid by BPA in future years. BPA has not deferred such payments since 1983.

Customers

BPA sells power and related services to four main types of customers: Northwest publicly owned utilities, direct-service industries, Northwest investor-owned utilites (IOUs) and other regional and extra regional customers. BPA also sells small amounts of power to several federal agencies within the region. The revenue derived from these customers provides BPA with a large portion of the funds needed to pay its costs. BPA sells transmission and related services under open access tariffs to a broad variety of power generators, including wind generators, marketers and power purchasers. The Revenues by Customer Class Table at the end of this section includes the following classifications.

Sales within the Northwest region

Northwest publicly owned utilities

Qualifying public utility districts, municipalities and consumer-owned electric cooperatives within the region are entitled to a statutory preference and priority in the purchase of available FCRPS power. These customers have what is referred to as public preference. They are eligible to purchase power at BPA's priority firm rate for most of their loads. As a group, publicly owned utilities constitute BPA's largest customer base in terms of number, megawatt sales and revenues.

Direct-service industries

BPA is not required to do so, but may offer to sell power for direct consumption to a limited number of existing DSIs within the region.

Northwest investor-owned utilities

BPA provides some firm power to Northwest IOUs. This is power not sold under the public preference priority rate. BPA also sells substantial amounts of peaking capacity to Northwest IOUs during cold periods. As part of its Subscription Strategy, BPA entered into certain agreements, as amended, with the IOUs in settlement of BPA's statutory obligation to provide benefits under the Residential Exchange Program for specified periods that began Oct. 1, 2001.

Revenues from Northwest IOUs fluctuate with streamflows in the Columbia River Basin. Streamflows directly impact the amount of surplus energy available for sale, the costs of generating power with alternative fuels, and ultimately the price BPA can obtain for these sales.

Sales outside the Northwest region

BPA sells secondary power to various buyers that is in excess of what is needed to serve firm load obligations in the region. Revenue from sales outside the Northwest are highly dependent upon streamflows in the Columbia River Basin which affect the amount of secondary energy available for sale, and upon the costs of generating power with alternative fuels, which affect the price BPA can obtain for its exported non-firm energy and surplus firm power. As is the case with revenues from Northwest IOUs, revenues from sales outside the Northwest region fluctuate with streamflows in the Columbia River Basin.

Bookouts

In fiscal year 2004, BPA's total operating expenses and revenues from electricity sales reflected for the first time the impacts of certain newly adopted accounting guidance from the Emerging Issues Task Force (EITF) of the Financial Accounting Standards Board (FASB). Under this guidance (referred to herein as EITF 03-11), which BPA adopted as of Oct. 1, 2003, both revenues and expenses associated with non-trading energy activities that are "booked out" (settled other than by the physical delivery of power) are to be reported on a net basis in both operating revenues and purchased power expense. Formerly, such bookouts were to be treated on a gross basis. Application of the new guidance thus decreased both operating revenues from power sales and purchase power expense in fiscal years 2005 and 2004 by $239 million and $212 million, respectively, from what they otherwise would have been absent application of the guidance. The accounting treatment under EITF 03-11 had no effect on net revenue, cash flows or margins. Prospective application of EITF 03-11 will continue to result in a significant decrease in reported non-trading wholesale energy sales and purchases and related amounts when compared with financial statements issued prior to the application of the guidance. Prior to Oct. 1, 2003, such settlements were recorded on a gross basis in both revenues and purchased power expense. Amounts for periods prior to Oct. 1, 2003, have not been reclassified. Therefore both revenues and purchased power expense are reported on a gross basis for fiscal year 2003. Although determination of the effect of the change on prior years' reported revenues and expenses is not practicable, the change has no impact on reported net revenues.

Transmission

BPA receives revenues by providing transmission and other related services. Transmission revenues fluctuate with weather conditions within the region and outside of the region, hydro conditions related to secondary power sales and outage requests for construction and maintenance purposes. Over the past few years, secondary sales of transmission service have grown. Customers with excess capacity are able to sell that capacity to other users at a rate below BPA's rate for short-term, non-firm transmission service. BPA is required to provide transmission service to generators and marketers under the same open access tariffs it uses to charge PBL and other transmission customers.

Other revenues

Derivative mark-to-market accounting adjustments and other miscellaneous revenues are included in this category.

U.S. Treasury credits for fish

The Northwest Power Act obligated the BPA administrator to make expenditures for fish and wildlife protection, mitigation and enhancement for both power and non-power purposes, on a reimbursement basis. The Northwest Power Act also specified that consumers of electric power, through their rates for power services "shall bear the costs of measures designed to deal with adverse impacts caused by the development and operation of electric power facilities and programs only." Section 4(h)(10)(C) of the Northwest Power Act was designed to ensure that the costs of mitigating these impacts are properly accounted for among the various purposes of the hydroelectric projects. In the early 1990s, BPA, the U.S. Treasury and the Office of Management and Budget agreed to a crediting mechanism whereby BPA reduces its cash payments to the U.S. Treasury by an amount equal to the mitigation measures funded on behalf of the non-power purposes. BPA has taken U.S. Treasury credits for fish annually since 1995.

The following table summarizes revenues by customer class for the three years ended Sept. 30, 2005, 2004 and 2003.

Revenues by Customer Class

Federal Columbia River Power System
For the years ended Sept. 30 — thousands of dollars

	2005	2004	2003
Sales of electric power:			
Sales within the Northwest region			
Northwest publicly owned utilities	**$1,717,063**	$1,737,895	$1,723,341
Direct-service industries	**82,454**	92,424	18,494
Northwest investor-owned utilities	**390,511**	363,201	436,702
Sales outside the Northwest region	**600,765**	489,063	628,243
Bookouts	**(238,847)**	(212,155)	—
Total sales of electric power	**2,551,946**	2,470,428	2,806,780
Transmission	**527,383**	535,936	552,718
Other revenues	**131,054**	114,547	77,722
U. S. Treasury credits for fish	**57,700**	77,000	174,884
Total operating revenues	**$3,268,083**	$3,197,911	$3,612,104

Liquidity and Capital Resources

At Sept. 30, 2005, the FCRPS ending cash balance was $652 million. Of this, BPA's year-end cash was $548 million and deferred borrowing authority was $6 million. Deferred borrowing represents amounts that BPA is authorized to borrow from the U.S. Treasury for expenditures that BPA has incurred but not borrowed for to date. For fiscal years 2004 and 2003 BPA's year-end cash and deferred borrowing authority were $587 million and $51 million, and $408 million and $103 million, respectively.

Operating activities

Cash provided by operating activities of the FCRPS increased $11 million to $677 million for the year ended Sept. 30, 2005, compared to $666 million for the year ended Sept. 30, 2004.

Cash provided by operating activities decreased $208 million to $666 million for the year ended Sept. 30, 2004 compared to $874 million for the year ended Sept. 30, 2003.

For both periods, the change in operating cash flow primarily reflects differences in the timing of collecting receivables and payments of accounts payable and accrued liabilities.

Investment activities

Cash used for investment activities of the FCRPS decreased $152 million to $494 million for the year ended Sept. 30, 2005, primarily from lower capital expenditures for federal utility plant, when compared to the prior year. Capital expenditures for federal utility plant totaled $425 million for the year ended Sept. 30, 2005, compared to $576 million for the year ended Sept. 30, 2004. The decrease was primarily a result of the reduction in such expenditures upon completion of TBL projects including Coulee-Bell and substantial completion of the Schultz-Wautoma project in the year ended Sept. 30, 2005.

Cash used for investment activities decreased $10 million to $647 million for the year ended Sept. 30, 2004, primarily reflecting lower capital expenditures for nonfederal projects, when compared to the prior year. Capital expenditures for nonfederal utility plant totaled $48 million for the year ended Sept. 30, 2004, compared to $85 million for the year ended Sept. 30, 2003. The decrease primarily reflected nonfederal debt financing activities and incremental investments at CGS.

Financing activities

BPA manages the FCRPS debt portfolio to meet the objectives of: (1) minimizing the cost of debt to BPA's ratepayers; (2) maximizing BPA's access to its lowest cost capital sources to meet future capital needs at the lowest cost to ratepayers; and (3) maintaining sufficient financial flexibility to meet BPA's financial requirements.

In the spring of 2000, BPA presented a debt optimization proposal to Energy Northwest. The proposal, which was agreed to by Energy Northwest, involves the extension of the final maturity of debt issued for the Columbia Generating Station. In September 2001, Energy Northwest's Executive Board adopted an updated refunding plan in which it also incorporated an increase in the average life of outstanding bonds issued for Projects 1 and 3 as a program objective for any future refinancing of such bonds.

Implementing the BPA proposal is intended to provide BPA with cash flow flexibility to allow BPA to advance the amortization of BPA's high-interest federal debt and to reduce BPA's overall fixed costs. Under the debt optimization proposal through Sept. 30, 2005, approximately $1.8 billion in bonds issued by Energy Northwest have been refinanced with new bonds having final maturities in calendar years 2013-2018. BPA expects that Energy Northwest will continue to undertake similar refinancing through at least fiscal year 2008. As a result of the actions taken under the BPA proposal, BPA prepaid appropriations and outstanding bonds issued to the U.S. Treasury by $313 million, $346 million and $315 million in the fiscal years ended Sept. 30, 2005, 2004 and 2003, respectively. Of the $313 million in Treasury prepayments in fiscal year 2005 about $40 million of such prepayments arose from debt optimization refinancing by Energy Northwest in fiscal year 2002 and about $273 million arose from debt optimization refinancing by Energy Northwest in fiscal year 2005.

In addition to refinancing actions under the debt optimization proposal in fiscal year 2005, Energy Northwest issued $92 million in new debt backed by BPA to meet future fuel needs for the CGS reactor. BPA together with the City of Eugene in Oregon, acting by and through the Eugene Water and Electric Board also issued $27 million solely as an economic refunding to lower debt service, and not as part of the BPA proposal.

In fiscal year 2004, BPA through its nonfederal partners refinanced or restructured approximately $606 million in its nonfederal debt portfolio. In addition, in fiscal year 2004, Northwest Infrastructure Financing Corporation (NIFC), a Delaware special purpose corporation, issued $119.6 million in taxable bonds to finance the Schultz-Wautoma transmission line. The bonds issued by NIFC are secured by lease rental payments by BPA under a lease-purchase agreement with BPA.

Credit ratings

BPA maintained high credit ratings on nonfederal debt backed by BPA with the three bond rating agencies covering BPA. In fiscal year 2005, Moody's maintained its credit rating on BPA-backed third party bonds at Aaa, and Standard & Poor's and Fitch maintained their ratings on BPA-backed third party bonds at AA minus.

Treasury payment

BPA paid the U.S. Treasury $1.088 billion for fiscal year 2005, making it the 22nd consecutive year in which BPA has made its payments on time and in full. The fiscal year 2005 payments included $616.5 million in principal and $400.7 million in interest for bonds issued to the U.S. Treasury and for the appropriated federal investment in the FCRPS. BPA also paid the U.S. Treasury $71 million in other obligations, including $26.5 million to fully fund post-retirement benefit programs for FCRPS employees. Payments made in fiscal years 2004 and 2003 were $1.053 billion and $1.057 billion, respectively. This year's principal payment also included $313 million to repay federal appropriations and bonds issued to the U.S. Treasury in excess of those scheduled in FERC filings, bringing cumulative advance payments to $1.459 billion.

BPA borrowing authority

In February 2003, Congress enacted and the President signed into law a $700 million increase in the amount of bonds issued to the U.S. Treasury that BPA may have outstanding at any given time. The new law increased to $4.45 billion the aggregate principal amount of bonds BPA is authorized to sell to the U.S. Treasury and to have outstanding at any one time. The new increment of available bonds outstanding is to be used for BPA's transmission capital program and to implement BPA's authorities under the Northwest Power Act.

Of the $4.45 billion in borrowing authority that BPA has with the U.S. Treasury, $2.78 billion of bonds were outstanding as of Sept. 30, 2005. Under current law, none of this U.S. Treasury borrowing authority may be used to acquire electric power from a generating facility having a planned capability of more than 50 average megawatts. Of the $4.45 billion in U.S. Treasury borrowing authority, $1.25 billion is available for renewable resources and conservation purposes and the remaining $3.2 billion is available for BPA's transmission capital program and to implement BPA's authorities under the Northwest Power Act.

The interest on BPA's outstanding bonds issued to the U.S. Treasury is set at rates comparable to the rates prevailing in the market for similar bonds issued by government corporations. As of Sept. 30, 2005, the interest rates on the outstanding bonds ranged from 2.30 percent to 8.55 percent with a weighted average interest rate of approximately 4.8 percent. The terms of the outstanding bonds vary from three to 34 years. The term of the bonds is limited by the average expected service life of the associated investment: 40 years for transmission facilities, 75 years for Corps and Reclamation capital investments, up to 20 years for conservation investments and 15 years for fish and wildlife projects. Bonds can be issued with call options. At Sept. 30, 2005, BPA had seven callable bonds on its books totaling $353.9 million.

Contractual Obligations and Federal Payments

As of Sept. 30 — thousands of dollars

	2006	2007	2008	2009	2010	2011+	Total
Federal appropriations*	$ 325,860	$ 285,824	$ 260,691	$258,901	$ 274,641	$ 8,937,469	$10,343,386
Bonds issued to U.S. Treasury*	584,930	576,961	501,716	238,357	95,445	911,433	2,908,842
Nonfederal projects debt*	559,296	632,848	626,128	629,188	640,375	6,047,225	9,135,060
Asset Retirement Obligations*	7,630	7,869	8,608	9,352	10,195	355,464	399,118
IOU exchange benefits	357,000	125,437	125,437	125,437	125,438	125,438	984,187
Purchase power commitments	559,067	19,472	18,847	53,102	53,102	54,027	757,617
Irrigation assistance	—	—	2,950	6,590	—	657,693	667,233
Additional post-retirement contributions	23,200	21,100	18,000	30,554	31,195	—	124,049
Total contractual obligations	$ 2,416,983	$1,669,511	$1,562,377	$1,351,481	$1,230,391	$17,088,749	$25,319,492

** Amounts shown include interest.*

Contractual obligations and federal payments

The table on page 40 shows the FCRPS' contractual obligations and federal payments as of Sept. 30, 2005.

Results of Operations

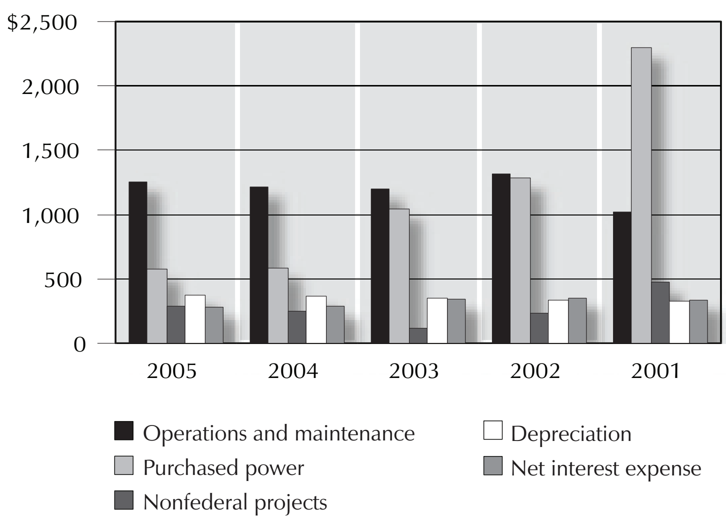
2005 compared to 2004

The fiscal year ended Sept. 30, 2005, total operating revenues were $3.268 billion, an increase of $70 million from the previous year. Sales from electricity and transmission sales for the fiscal year ended Sept. 30, 2005, increased approximately $78 million from the fiscal year 2004 levels. The increased sales from electricity and transmission sales resulted from higher discretionary sales of surplus power outside the region. The Statement of Financial Accounting Standards (SFAS) 133, "Accounting for Derivative Instrument and Hedging Activities," derivative mark-to-market amount increased $5 million, miscellaneous revenues increased $6 million, and U.S. Treasury credits for fish under Northwest Power Act section 4(h)(10)(C) decreased $19 million, in the fiscal year ended Sept. 30, 2005, when compared to the prior year.

In total, operating expenses increased $95 million, or 4 percent, in fiscal year 2005 when compared to the prior year. Operations and maintenance increased $45 million, or 4 percent, from the fiscal year ended Sept. 30, 2004. This increase reflects the effects of higher operating costs at the CGS of $21 million, mainly for nuclear fuel, and increased IOU monetary benefits of $18 million. Operating expenses in the year ended Sept. 30, 2005, amounts also reflect that purchased power decreased $2 million, or less than 1 percent, compared to the fiscal year ended Sept. 30, 2004, and that nonfederal projects debt service expense increased $43 million, or 17 percent. The nonfederal project debt service expense increased in part because the Energy Northwest fiscal year 2004 operating budgets included approximately $79 million that was made available when reserve funds for certain Energy Northwest net-billed bonds were replaced with surety agreements. The surety

Expenses by Category

millions of dollars



agreements were used to reduce fiscal year 2004 net-billing requirements for nonfederal projects debt service. In addition, federal projects depreciation increased $9 million, or 3 percent, primarily due to the energization of the Grand Coulee-Bell transmission line.

Net interest expense for the year ended Sept. 30, 2005, decreased $8 million, or 3 percent, compared to the prior year. Interest on appropriated funds decreased due to lower principal owed to the U.S. Treasury. Interest on bonds issued to the U.S. Treasury decreased as the weighted average interest rate declined from 5.3 percent at the beginning of fiscal year 2004 to 4.9 percent at the beginning of fiscal year 2005. This interest expense also decreased as the income earned on BPA's cash account at the U.S. Treasury increased with higher average cash balances. BPA reports interest expense on long-term debt net of the interest income earned. The decrease in interest expense was partially offset by decreased allowance for funds used during construction due to lower construction work in progress balances.

Net revenues were $487 million in fiscal year 2005, a decrease of $18 million, or 4 percent, from fiscal year 2004 as a result of the factors discussed above.

2004 compared to 2003

The fiscal year 2004 total operating revenues were $3.198 billion, a decrease of $414 million, from the previous year due to declining sales of $355 million, SFAS 133 derivative mark-to-market increasing $34 million, miscellaneous revenues increasing $4 million and U.S. Treasury credits for fish decreasing $98 million.

As a result of the EITF 03-11 adoption discussed above in "Bookouts," sales and purchased power expenses for the year both decreased by $212 million. The remaining $143 million decline in sales was the result of expiring purchase power commitments of nearly 400 average megawatts and a corresponding reduction in sales, reduced Load-Based Cost Recovery Adjustment Clause (LB CRAC) percentage for April through September, and lower non-firm transmission and other revenues as a result of changed customer marketing practices.

U.S. Treasury credits for fish operations decreased from $175 million to $77 million in fiscal year 2004. The fiscal year 2003 credit included $79 million from the Fish Cost Contingency Fund, which became fully depleted in fiscal year 2003. Conditions were drier prior to March 2003 resulting in higher credit estimates when compared to the same period of fiscal year 2004.

In fiscal year 2004, total operating expenses were $2.409 billion, a decrease of $302 million compared to fiscal year 2003 due to operations and maintenance increasing $13 million, purchased power decreasing $461 million, nonfederal projects increasing $129 million and federal projects depreciation increasing $16 million.

As previously discussed, purchased power expenses reflects the Oct. 1, 2003, adoption of EITF 03-11. Purchased power decreased $119 million as augmentation contracts expired and BPA negotiated the termination of several sales and purchase power commitments in 2003 for fiscal year 2004 approximating $78 million. The balance of the change was due to decreased purchases.

Debt service for nonfederal projects increased $129 million, or 108 percent, primarily because fiscal year 2003 amortization of debt for Energy Northwest net-billed projects was comparatively low as a result of the debt optimization program and the embedded amortization schedule for such debt. In fiscal year 2003 Energy Northwest debt service was also paid in part by funds made available when reserve funds for certain Energy Northwest net-billed bonds were replaced with surety agreements.

Interest on bonds issued to the U.S. Treasury decreased $56 million as the weighted average interest rate declined from 6 percent at the beginning of fiscal year 2003 to 5.3 percent at the beginning of fiscal year 2004. The decreased weighted average interest rate was due to two factors: the debt optimization program and the low interest rate environment. Through the debt optimization program, BPA paid off bonds issued to the U.S. Treasury bearing relatively high interest rates and issued nonfederal projects debt with very low interest rates.

To a lesser degree, interest on bonds issued to the U.S. Treasury decreased as the income earned on BPA's cash account at the U.S. Treasury increased with higher cash balances. BPA reports interest expense on bonds issued to the U.S. Treasury net of the interest income earned. Net interest expense for fiscal year 2004 decreased $61 million from fiscal year 2003.

As a result of the factors discussed above, net revenues were $504 million in fiscal year 2004, a decrease of $51 million or 9 percent from fiscal year 2003.

Fish and Wildlife

The Northwest Power Act directs BPA to protect, mitigate and enhance fish and wildlife resources to the extent they are affected by federal hydroelectric projects on the Columbia River and its tributaries. BPA makes expenditures and incurs other costs for fish and wildlife consistent with the Northwest Power Act and the Pacific Northwest Power and Conservation Council's Columbia River Basin Fish and Wildlife Program. In addition, in the wake of certain listings of fish species under the Endangered Species Act (ESA) as threatened or endangered, BPA is financially responsible for expenditures and other costs arising from conformance with the ESA and certain biological opinions prepared by the National Oceanic and Atmospheric Administration Fisheries and the Fish and Wildlife Service in furtherance of the ESA.

BPA typically funds fish and wildlife mitigation through several mechanisms. Since the creation of the FCRPS, BPA has repaid the U.S. Treasury the share of the costs of mitigation by the Corps and Reclamation that is allocated by law or pursuant to policies promulgated by FERC's predecessor to the federal projects' power purpose. These measures mitigate for the impact on fish and wildlife of the construction and operation of hydroelectric dams of the FCRPS.

BPA also implements and funds measures proposed in the Council's fish and wildlife program, which the Council periodically amends. The program calls for a variety of mitigation measures from habitat protection to mainstem Columbia River and Snake River flow targets. Such measures affect the operation for the FCRPS and require BPA to purchase power to fulfill contractual demands or to spill water and thereby forgo generation of electricity. The financial impacts of these investments in fish and wildlife are counted as measures funded by BPA. Some of the program's measures, especially those designed to benefit species not listed under the ESA, are in addition to ESA-directed measures. However, with respect to the measures for listed species in the Council's program, many of the measures identified in the FCRPS biological opinions and in the Council's program overlap. BPA uses a comprehensive approach to implementation described as integrated, meaning the ESA requirements of the FCRPS biological opinions are incorporated with the broad fish and wildlife protection, mitigation and enhancement objectives of the Council's program, consistent with the Northwest Power Act.

BPA's fish and wildlife costs fall into two main categories, direct costs and operational impacts.

Direct costs include integrated program costs, which are the costs to BPA of implementing the Council's program, and which include expense and capital components for ESA-related and non-ESA-related measures that are located at sites away from the FCRPS dams; expenses for recovery of capital, which include depreciation, amortization and interest expenses for fish and wildlife capital investments by the Corps, Reclamation and BPA; and, other entities' operation and maintenance, which include fish and wildlife O&M costs of the U.S. Fish and Wildlife Service for the Lower Snake River Hatcheries and of the Corps and Reclamation for FCRPS projects.

Operational impacts include replacement power purchase costs and foregone power revenues. Replacement power purchase costs are the costs of certain power purchases made by BPA that are attributable to river operations in aid of fish and wildlife. To determine these costs in a given year, BPA compares the actual hydroelectric generation in such year against the hydroelectric generation that would have been produced had the hydroelectric system been operated without any fish and wildlife operating constraints. To the extent this comparison indicates BPA made a power purchase to meet load — a purchase BPA would not have had to make had the river been operated free of fish constraints — BPA accounts for such value as a fish and wildlife cost. Foregone power revenues, are revenues that would have been earned absent changes in hydroelectric system operations attributable to fish and wildlife.

Fish and wildlife estimated costs are shown in the following table.

Fish and Wildlife

Federal Columbia River Power System
For the years ended Sept. 30 — thousands of dollars

	2005	2004	2003
Foregone power revenues	**$ 182,000**	$ 22,000	$ 79,000
Direct costs and replacement power purchases	**394,000**	479,000	451,000
Total fish and wildlife	**$ 576,000**	$501,000	$530,000

Environmental Matters

From time to time, there are sites where BPA, the Corps or Reclamation have been or may be identified as a potential responsible party. Costs associated with cleanup of those sites are not expected to be material to the FCRPS financial statements and would be recoverable through future rates.

Impact of Recently Issued Accounting Standards

As discussed above, BPA adopted EITF 03-11 in fiscal year 2004 which resulted in both operating revenues from power sales and purchase power expense being reduced the same amounts from what they otherwise would have been absent application of the guidance. The accounting treatment under EITF 03-11 had no effect on net revenue, cash flows or margins.

In January 2003, the FASB issued FASB Interpretation No. 46 (FIN 46), "Consolidation of Variable Interest Entities — an interpretation of ARB No. 51." In December 2003, FIN 46 was reissued as FIN 46R, which contained revisions to address certain implementation issues. FIN 46 clarifies the application of Accounting Research Bulletin (ARB) No. 51, "Consolidated Financial Statements," to certain entities in which equity investors do not have sufficient equity at risk for the entity to finance its activities without additional subordinated financial support from other parties. The interpretation differentiates between an entity with a majority voting interest (the previous requirement under ARB No. 51) and entities that have controlling financial interest through other arrangements that may not involve any voting interests and how these types of entities (variable interest entities) may need to be consolidated. For non-public entities there is no distinction in effective dates for variable interest entities (VIEs) and non-VIEs. The application of FIN 46 is required for all entities created before Dec. 31, 2003, by no later than the beginning of the first interim or annual reporting period beginning after Dec. 15, 2003. For entities created after Dec. 31, 2003, application of FIN 46 is required as of the date they first become involved with the respective entities. NIFC is the FCRPS' only VIE and it has been consolidated into the BPA financial statements for fiscal years 2004 and 2005. The impact on net revenues is shown in the following table.

Impact of Recently Issued Accounting Standards

Federal Columbia River Power System
For the years ended Sept. 30 — thousands of dollars

	2005	2004	2003
Net revenues prior to adoption of:	**$ 486,904**	$ 504,439	$ 555,424
FIN 46	**(34)**	(24)	—
Net revenues	**$ 486,870**	$ 504,415	$ 555,424

Forward-looking Information

President's fiscal year 2006 budget

The President's fiscal year 2006 budget includes a proposal for legislation that calls "for certain non traditional financing transactions that are entered into after the date the legislation is enacted and that are similar to debt-like transactions to be treated as debt and counted toward [BPA's] statutory debt limit." The President's administration has not yet sought to introduce draft legislation to effect this proposal in Congress, thus the exact nature of the proposal is uncertain. Nonetheless, the budget provides that the proposal would only affect those transactions occurring after enactment of the legislation. In addition, the Department of Energy has agreed that the proposed legislation will not affect BPA's ability to participate in the refinancing of debt it secures pursuant to transactions that BPA entered into prior to the date the proposed legislation takes effect.

The President's fiscal year 2006 budget also includes a proposal for legislation "to very gradually bring [the federal power marketing administrations', including BPA's] electricity rates closer to average market rates throughout the country." The President's administration has not yet sought to introduce draft legislation to effect this proposal in Congress, thus, the exact nature of the proposal is uncertain. BPA is unable to predict whether such legislation will be introduced in, or enacted into law by, Congress.

Fish and wildlife

BPA expects to continue to support substantial fish and wildlife mitigation and protection costs in the future. BPA is unable to predict the future range of such costs.

Critical Accounting Policies

BPA's rates are designed to recover its cost of service. In connection with the rate-setting process, certain costs or credits may be included in rates for recovery over a period of time that differs from normal treatment under generally accepted accounting principles. Under those circumstances, regulatory assets or liabilities are recorded and such costs or credits are amortized over the periods they are included in rates in accordance with SFAS 71, "Accounting for the Effects of Certain Types of Regulation."

In order to defer incurred costs under SFAS 71, a regulated entity must have the statutory authority to establish rates that recover all costs and rates so established must be charged to and collected from customers. Due to increasing competitive pressures, BPA may be required to seek alternative solutions in the future to avoid raising rates to a level that is no longer competitive. If BPA's rates should become market-based, SFAS 71 would no longer be applicable, and any deferred costs and revenues under that standard would be expensed and recognized, respectively, in the Statement of Revenues and Expenses in that period. Amortization of these are reflected in the Statements of Revenues and Expenses. BPA does not earn a rate of return on its regulatory assets.

See Note 1, Rates and Regulatory Authority, for a table summarizing regulatory assets and liabilities as of Sept. 30, 2005, and 2004.

Modified Net Revenues

Modified net revenues are net revenues after removing the effects of SFAS 133 and nonfederal debt management actions that differ from rate case assumptions. 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. Calculations similar to modified net revenues were developed as part of the initial rates for the current period and are used to determine the thresholds for two of the PBL Cost

Recovery Adjustment Clauses – the Financial-Based (FB CRAC) and the Safety Net (SN CRAC). The following table demonstrates the calculation for modified net revenues. The primary change in modified net revenues from fiscal year 2003 through fiscal years 2004 and 2005 is due to the increase in nonfederal projects debt service as discussed in the Results of Operations.

Modified Net Revenues

Federal Columbia River Power System
For the years ended Sept. 30 — thousands of dollars

	2005	2004	2003
Net Revenues	**$486,870**	$504,415	$555,424
SFAS 133 derivative mark-to-market gain	**(94,596)**	(89,452)	(55,265)
Nonfederal debt management actions	**(266,139)**	(348,636)	(463,285)
Modified net revenues	**$126,135**	$66,327	$36,874

Market Risk

Risk Management

BPA's Office of the Chief Risk Officer was formed at the start of fiscal year 2004. The Transacting Risk Management Committee has responsibility for the oversight of market risk and determines the risk policy and control environment at BPA. Experienced business and risk managers use the results of the hydro supply scenario and simulation analyses and the market price risk measures in conjunction with their professional judgment to capture additional market-related risks, including credit and event risk.

Due to both the operational risk posed by fluctuations in river flows affecting the hydroelectric generation supply capability and the commodity price risk, net revenues effects from underlying surplus or deficit energy positions are inherently uncertain.

Commodity Price Risk and Volumetric Risk

Primarily due to the periodic variation in the available energy from its hydroelectric generation capacity, BPA enters into short-term and forward sales and purchase agreements for electricity in the wholesale markets to balance its energy supply and demand. Fluctuations in the electric market prices in the Pacific Northwest can affect the value of energy inventory being bought and sold as well as the value of prior purchase and sale contracts. This is referred to as commodity price risk. In fiscal year 2005, there was a net surplus and sale of energy, which was in excess of that needed to serve firm load obligations in the service region.

BPA measures the market price risk in its portfolio on a daily, weekly and monthly basis using net revenue at risk (NRaR), mark-to-market, value at risk (VaR), Monte Carlo simulation and other methodologies depending on the portfolio segment in question. The quantification of market risk using these methods provides a consistent measure of risk across the energy market in which BPA buys and sells. The use of these methods requires a number of key assumptions including hydro/price correlations, the selection of a confidence level for expected losses, the holding period for liquidation and the treatment of risks outside the methodology, including credit risk and event risk. These methods provide an estimate of reasonably possible net revenue outcomes that could be recognized on its portfolios assuming hypothetical movements in future market prices. In response to market price risk, futures, forwards, swaps and options may be used to alter BPA's exposure to price fluctuations.

As of Sept. 30, 2005, BPA's five-day, 95 percent confidence level diversified VaR for power futures, forwards, swaps and options contracts over the next 12 months was approximately $6.9 million. In addition, as of Sept. 30, 2005, BPA's 5 percent confidence level NRaR calculation secondary power net revenues over the next 12 months, which incorporates both price and volumetric uncertainty, was $808 million.

Besides using market price risk measures, BPA measures the effects of volumetric risk using both scenario analysis and Monte Carlo simulation to estimate the economic impact of a sudden change in supply or price. Unlike many of its industry counterparts, BPA's principal market activity is the sale of surplus inventory rather than the purchase and sale of electricity to earn trading revenues. Therefore, the tests critical to trading organizations (i.e. amount of risk to carry over very short time frames) are considered less important than regular and rigorous analysis of the consequences of a range of hydro supply conditions and prolonged holding periods.

Credit Risk

Credit risk relates to the risk of loss that might occur as a result of non-performance by counterparties of their obligations to make or take delivery of electricity. BPA's counterparties are generally large and stable and do not represent a significant concentration of credit risk. During fiscal year 2005, BPA experienced no significant losses as a result of any customer defaults or bankruptcy filings. Credit risk is mitigated at BPA by reviewing counterparties for creditworthiness, establishing credit limits, and monitoring credit exposure on a daily basis, and performing Credit Value at Risk (CVaR) measurements for forward power transactions on a weekly basis. In order to further manage credit risk, BPA obtains credit support such as letters of credit and third-party guarantees from some counterparties. Counterparties are monitored closely for changes in financial condition and credit reviews are updated regularly.

As of Sept. 30, 2005, BPA had $306.6 million in credit exposure to purchase and sale contracts taking into account netting rights. BPA uses internally developed, commercially appropriate rating methodologies, credit scoring models, publicly available information, and external ratings from major credit rating agencies to determine the public rating equivalent grade of counterparties. As of Sept. 30, 2005 BPA's credit exposure, net of collateral, to sub-investment grade counterparties was less than 1 percent of total outstanding credit exposures. The Agency's top five credit exposures were $262 million, or 82 percent, of the total credit exposure. This relatively high concentration of credit risk has been substantially ameliorated by letters of credit posted by creditworthy banks.

Interest Rate Risk

BPA does not issue variable rate debt to the U.S. Treasury and is not exposed to substantive risk resulting from changes in interest rates as a result of its backing of the variable-rate debt issued by Energy Northwest.

Of the $846 million of Energy Northwest variable rate debt outstanding as of Sept. 30, $500 million has been swapped into synthetic fixed rate debt as described in footnote 1. Under these swap agreements, BPA pays the counterparties a fixed rate and receives a variable rate which is 68 percent of LIBOR. Although not a perfect match, the amount BPA receives is intended to offset the variable rate paid on the $500 million in bonds issued by Energy Northwest.

The remaining variable rate debt approximately matches the variable rate assets held at EN. Although the asset amount fluctuates throughout the year, an approximate match is maintained over time. The combined effect of these transactions is that BPA has virtually no net variable rate debt exposure and therefore, there is no substantive interest rate exposure on Bonneville-backed variable rate debt.

Rates

BPA's rates are subject to the regulatory oversight described in the first note to the financial statements and are designed to recover its cost of service.

Selected Quarterly Information

Federal Columbia River Power System

3 months ended — thousands of dollars

	December 31	March 31	June 30	September 30	Totals
2005					
Revenues	**$776,805**	**$805,778**	**$701,765**	**$ 889,139**	**$3,173,487**
SFAS 133 mark-to-market	**(8,826)**	**15,040**	**1,914**	**86,468**	**94,596**
Operating revenues	**767,979**	**820,818**	**703,679**	**975,607**	**3,268,083**
Operating expenses	**587,015**	**622,066**	**642,559**	**652,289**	**2,503,929**
Net interest expenses	**71,491**	**70,697**	**67,442**	**67,654**	**277,284**
Net revenues (expenses)	**$109,473**	**$128,055**	**$ (6,322)**	**$ 255,664**	**$ 486,870**
2004					
Revenues	$823,281	$755,437	$702,847	$ 826,894	$3,108,459
SFAS 133 mark-to-market	(1,210)	29,623	85,396	(24,357)	89,452
Operating revenues	822,071	785,060	788,243	802,537	3,197,911
Operating expenses	577,734	532,174	611,850	686,887	2,408,645
Net interest expenses	74,576	75,169	67,501	67,605	284,851
Net revenues	$169,761	$177,717	$108,892	$ 48,045	$ 504,415
2003					
Revenues	$898,748	$901,112	$760,233	$ 996,746	$3,556,839
SFAS 133 mark-to-market	47,134	(25,904)	24,712	9,323	55,265
Operating revenues	945,882	875,208	784,945	1,006,069	3,612,104
Operating expenses	698,279	740,185	490,416	782,209	2,711,089
Net interest expenses	87,712	85,144	81,546	91,189	345,591
Net revenues	$159,891	$ 49,879	$212,983	$ 132,671	$ 555,424

Combined Balance Sheets

Federal Columbia River Power System
As of Sept. 30 — thousands of dollars

Assets

	2005	2004
Federal utility plant		
Completed plant	**$12,722,386**	$12,243,684
Accumulated depreciation	**(4,453,745)**	(4,357,496)
	8,268,641	7,886,188
Construction work in progress	**1,152,978**	1,401,793
Net federal utility plant	**9,421,619**	9,287,981
Nonfederal generation	**2,389,445**	2,368,314
Current assets		
Cash	**651,740**	654,242
Accounts receivable, net of allowance	**88,184**	91,517
Accrued unbilled revenues	**208,801**	158,074
Materials and supplies, at average cost	**75,073**	81,246
Prepaid expenses	**321,032**	331,383
Total current assets	**1,344,830**	1,316,462
Other assets		
Regulatory assets	**5,509,596**	5,584,062
Nonfederal nuclear decommissioning trusts	**125,509**	111,941
Deferred charges and other	**234,773**	264,019
Total other assets	**5,869,878**	5,960,022
Total assets	**$19,025,772**	$18,932,779

The accompanying notes are an integral part of these statements.

Capitalization and Liabilities

	2005	2004
Capitalization and long-term liabilities		
Accumulated net revenues	**$ 1,334,294**	$ 847,424
Federal appropriations	**4,272,662**	4,339,288
Bonds issued to U.S. Treasury	**2,211,800**	2,461,800
Nonfederal projects debt	**6,286,559**	6,218,932
Total capitalization and long-term liabilities	**14,105,315**	13,867,444
Commitments and contingencies (Note 7)		
Current liabilities		
Federal appropriations	**68,939**	104,673
Bonds issued to U.S. Treasury	**565,000**	438,500
Nonfederal projects debt	**207,490**	234,896
Accounts payable and other	**322,497**	338,867
Total current liabilities	**1,163,926**	1,116,936
Other Liabilities		
Regulatory liabilities	**2,129,660**	2,161,401
IOU exchange benefits	**984,187**	1,008,296
Nonfederal nuclear asset retirement obligations	**160,600**	164,000
Deferred credits	**482,084**	614,702
Total other liabilities	**3,756,531**	3,948,399
Total Capitalization and Liabilities	**$19,025,772**	$18,932,779

The accompanying notes are an integral part of these statements.

Combined Statements of Revenues and Expenses

Federal Columbia River Power System
For the years ended Sept. 30 — thousands of dollars

	2005	2004	2003
Operating revenues			
Sales	**$ 3,051,976**	$ 2,973,496	$ 3,328,277
SFAS 133 derivative mark-to-market	**94,596**	89,452	55,265
Miscellaneous revenues	**63,811**	57,963	53,678
U.S. Treasury credits for fish	**57,700**	77,000	174,884
Total operating revenues	**3,268,083**	3,197,911	3,612,104
Operating expenses			
Operations and maintenance	**1,256,576**	1,211,802	1,198,521
Purchased power	**580,213**	582,129	1,043,009
Nonfederal projects	**291,540**	248,475	119,534
Federal projects depreciation and amortization	**375,600**	366,239	350,025
Total operating expenses	**2,503,929**	2,408,645	2,711,089
Net operating revenues	**764,154**	789,266	901,015
Interest expense			
Interest on federal investment:			
Appropriated funds	**192,110**	213,041	212,391
Bonds issued to U.S. Treasury	**102,077**	110,251	166,598
Allowance for funds used during construction	**(16,903)**	(38,441)	(33,398)
Net interest expense	**277,284**	284,851	345,591
Net revenues	**486,870**	504,415	555,424
Accumulated net revenues (expenses), Oct. 1	**847,424**	343,748	(211,676)
Irrigation assistance	**—**	(739)	—
Accumulated net revenues, Sept. 30	**$ 1,334,294**	$ 847,424	$ 343,748

The accompanying notes are an integral part of these statements.

Combined Statements of Changes in Capitalization and Long-Term Liabilities

Federal Columbia River Power System
Including current portions — thousands of dollars

	Accumulated Net (Expenses) Revenues	Appropriations	Bonds Issued to Treasury	Nonfederal Project Debt	Total
Balance at Sept. 30, 2003	$ 343,748	$4,680,960	$ 2,697,754	$ 6,286,593	$14,009,055
Federal appropriations:					
Increase for construction	—	78,047	—	—	78,047
Repayment of construction	—	(315,046)	—	—	(315,046)
Bonds issued to U.S. Treasury:					
Increase	—	—	480,000	—	480,000
Repayment	—	—	(277,454)	—	(277,454)
Nonfederal projects debt:					
Net increase	—	—	—	179,130	179,130
Repayment	—	—	—	(11,895)	(11,895)
Net revenues	504,415	—	—	—	504,415
Irrigation assistance	(739)	—	—	—	(739)
Balance at Sept. 30, 2004	$ 847,424	$4,443,961	$ 2,900,300	$ 6,453,828	$14,645,513
Federal appropriations:					
Increase for construction	**—**	**75,642**	**—**	**—**	**75,642**
Repayment of construction	**—**	**(178,002)**	**—**	**—**	**(178,002)**
Bonds issued to U.S. Treasury:					
Increase	**—**	**—**	**315,000**	**—**	**315,000**
Repayment	**—**	**—**	**(438,500)**	**—**	**(438,500)**
Nonfederal projects debt:					
Increase	**—**	**—**	**—**	**47,513**	**47,513**
Repayment	**—**	**—**	**—**	**(7,292)**	**(7,292)**
Net revenues	**486,870**	**—**	**—**	**—**	**486,870**
Balance at Sept. 30, 2005	**$1,334,294**	**$4,341,601**	**$ 2,776,800**	**$ 6,494,049**	**$14,946,744**

The accompanying notes are an integral part of these statements.

Combined Statements of Cash Flows

Federal Columbia River Power System
For the years ended Sept. 30 — thousands of dollars

	2005	2004	2003
Cash provided by operating activities			
Net revenues	**$ 486,870**	$ 504,415	$ 555,424
Non-cash items:			
Depreciation	**305,281**	294,975	269,957
Amortization	**70,319**	71,264	77,610
Amortization of capitalization adjustment	**(64,905)**	(68,566)	(67,703)
(Increase) decrease in:			
Receivables and unbilled revenues	**(47,394)**	87,594	(38,144)
Materials and supplies	**6,173**	3,061	801
Prepaid expenses	**10,351**	(43,316)	(2,372)
(Decrease) increase in:			
Accounts payable and other	**(16,370)**	(30,954)	26,396
Other	**(72,832)**	(152,601)	51,802
Cash provided by operating activities	**677,493**	665,872	873,771
Cash used for investment activities			
Investment in:			
Federal utility plant (including AFUDC)	**(424,735)**	(576,324)	(535,211)
Nonfederal projects	**(40,221)**	(47,650)	(85,050)
Conservation	**(14,825)**	(16,876)	(25,458)
Fish and wildlife	**(14,575)**	(5,849)	(11,156)
Cash used for investment activities	**(494,356)**	(646,699)	(656,875)
Cash provided by and used for financing activities			
Federal construction appropriations:			
Increase	**75,642**	78,047	99,418
Repayment	**(178,002)**	(315,046)	(61,060)
Bonds issued to U.S. Treasury:			
Increase	**315,000**	480,000	470,000
Repayment	**(438,500)**	(277,454)	(482,687)
Refinanced	**—**	—	(60,000)
Nonfederal debt:			
Increase	**47,513**	179,130	99,289
Repayment	**(7,292)**	(11,895)	(14,239)
Irrigation assistance	**—**	(739)	—
Cash (used for) provided by financing activities	**(185,639)**	132,043	50,721
(Decrease) Increase in cash	**(2,502)**	151,216	267,617
Beginning cash balance	**654,242**	503,026	235,409
Ending cash balance	**$ 651,740**	$ 654,242	$ 503,026

The accompanying notes are an integral part of these statements.

NOTES TO FINANCIAL STATEMENTS

1. Summary of Significant Accounting Policies

Principles of Combination

The Federal Columbia River Power System (FCRPS) combines the accounts of the Bonneville Power Administration (BPA), the accounts of generating facilities of the U.S. Army Corps of Engineers (Corps) and the Bureau of Reclamation (Reclamation) and the operation and maintenance costs of the U.S. Fish and Wildlife Service for the Lower Snake River Compensation Plan Facilities. Northwest Infrastructure Financing Corporation (NIFC), a "Special Purpose Corporation" formed on Dec. 17, 2003, has been consolidated with BPA for fiscal years 2004 and 2005. See Note 4 Nonfederal Projects and Related Debt.

BPA is the power marketing administration that purchases, transmits and markets power for the FCRPS. Each of the foregoing entities is separately managed and financed, but the facilities are operated as an integrated power system with the financial results combined as the FCRPS. The costs of multipurpose Corps and Reclamation projects are assigned to specific functions through a cost-allocation process. Only the portion of total project costs allocated to power is included in these statements.

FCRPS accounts are maintained in accordance with generally accepted accounting principles and the uniform system of accounts prescribed for electric utilities by the Federal Energy Regulatory Commission (FERC). FCRPS accounting policies also reflect specific legislation and executive directives issued by U.S. government departments. BPA is a unit of the U.S. Department of Energy; Reclamation and U.S. Fish and Wildlife are part of the U.S. Department of the Interior; and the Corps is part of the U.S. Department of Defense. U.S. government properties and income are tax-exempt. All material inter-company accounts and transactions have been eliminated from the combined financial statements.

Use of Estimates

The preparation of financial statements in conformity with generally accepted accounting principles requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities, the disclosure of contingent assets and liabilities at the date of the financial statements, and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates.

Reclassifications

Certain reclassifications were made to the fiscal years 2003 and 2004 combined financial statements from amounts previously reported to conform to the presentation used in fiscal year 2005. Such reclassifications had no effect on previously reported results of operations and cash flows.

Rates and Regulatory Authority

BPA's power and transmission rates are established in accordance with several statutory directives. Rates proposed by BPA are subjected to an extensive formal review process, after which they are proposed by BPA and reviewed by FERC. FERC's review is limited to three standards set out in the Pacific Northwest Electric Power Planning and Conservation Act (Northwest Power Act), 16 U.S.C. 839, and a standard set by the Energy Policy Act of 1992, 16 U.S.C. 824. FERC reviews BPA's rates for all firm power, non-firm energy and for transmission service. Statutory standards include a requirement that these rates be sufficient to assure repayment of the federal investment in the FCRPS over a reasonable number of years after first meeting BPA's other costs.

After final FERC approval, BPA's rates may be reviewed by the U.S. Court of Appeals for the Ninth Circuit (Ninth Circuit Court). Action seeking such review must be filed within 90 days of the final FERC decision. The Ninth Circuit Court may either confirm or reject a rate proposed by BPA. It is the opinion of BPA's General Counsel that, if a rate were rejected, it would be remanded to BPA for reformulation.

BPA submitted to FERC a Power Rate Filing in fiscal year 2001 for fiscal years 2002 through 2006. BPA submitted a Transmission and Ancillary Services Rate Filing in fiscal year 2003 for fiscal years 2004 through 2005 and in fiscal year 2005 for fiscal years 2006 through 2007. FERC granted final approval of the Power Rate Filing on July 21, 2003, 104 FERC 61,093 (2003). FERC granted final approval of BPA's Transmission and Ancillary Services Rate Filing for fiscal years 2004 through 2005 on Sept. 23, 2003, 104 FERC 62,207 (2003) and the Transmission and Ancillary Services Rate Filing for fiscal year 2006 through 2007 on Sept. 29, 2005, 112 FERC 62,258 (2005).

BPA has agreed that rates for the sale of power pursuant to its present contracts may not be revised until the current rate period expires on Sept. 30, 2006, except that rate levels may change under certain rate cost recovery adjustment clauses (CRACs). The CRACs are temporary upward adjustments to posted power prices if certain conditions occur. There are three CRACs, each triggered by a different set of conditions. The first is the Load-Based CRAC (LB CRAC), which triggers if BPA incurs costs for meeting or reducing loads that were not included in the rate case. The LB CRAC percentage changes every six months. The second is the Financial-Based CRAC (FB CRAC), which triggers if the generation function's forecast level of accumulated net revenues as modified in the General Rates Schedule Provisions (GRSP's) is below a predetermined threshold. The third is the Safety Net CRAC (SN CRAC), which triggers when BPA has missed or forecasts a 50 percent or greater probability of missing a payment to the U.S. Treasury or another creditor.

The LB CRAC percentage rate level increase was approximately 31.9 percent and 38.5 percent, respectively, for the six-month periods beginning Oct. 1, 2002, and April 1, 2003. The LB CRAC percentage increase was revised to approximately 21.3 percent and 24.6 percent, respectively, for the six-month periods beginning Oct. 1, 2003 and April 1, 2004. The LB CRAC percentage increase was revised to approximately 21.7 percent and 25.8 percent, respectively, for the six-month periods beginning Oct. 1, 2004 and April 1, 2005.

The August 2002 forecast of the generation function's accumulated net revenues as modified in the GRSP's for computing the FB CRAC thresholds triggered the FB CRAC, and resulted in a rate increase over base rates of approximately 11 percent for fiscal year 2003, approximately 12 percent for fiscal year 2004, and approximately 11 percent for fiscal year 2005 for most of the requirements rates. The increases were in addition to rate level increases under the LB CRAC.

The SN CRAC first triggered in fiscal year 2003, requiring an expedited rate proceeding resulting in a rate level increase that went into effect Oct. 1, 2003 through Sept. 30, 2004, of approximately 10 percent. The expedited rate case also enabled the recalculation of the FB CRAC thresholds. This ensures that the FB CRAC collects the maximum amount possible before the SN CRAC is calculated. The changes in the FB CRAC avoid cost shifts between the different customers to which the FB and SN CRACs apply. BPA submitted to FERC a separate power rate filing in fiscal year 2003 related to the design of the SN CRAC. FERC granted final approval of the filing on May 10, 2004, 107 FERC 61,138 (2004). The SN CRAC rate filing augments the power rates already approved for fiscal years 2002 through 2006 including rate level increases under the LB CRAC and FB CRAC. The SN CRAC was set to zero percent for FY 2005.

Rate adjustment clauses are calculated initially on forward-looking estimates of revenues and expenses, with adjustments made to future rates after financial results are known.

In addition to the CRACs, BPA established contracts and rates for a "Slice of the System Product." The basic premise of the product is that a purchaser pays a fixed percentage of BPA's power costs in exchange for a fixed percentage of generation output. Settlement of any over or under collection occurs in the subsequent year. For the fiscal year 2003 settlement, BPA recognized a $30.4 million liability which was paid in fiscal year 2004. For the fiscal year 2004 settlement, BPA recognized a receivable of $10.1 million which was received in fiscal year 2005. For the fiscal year 2005 settlement, BPA recognized a receivable of $43.3 million, to be received in fiscal year 2006.

BPA's rates are subject to the regulatory oversight described above and are designed to recover its cost of service. In connection with the rate-setting process, certain costs or credits may be included in rates for recovery over a period of time that differs from normal treatment under generally accepted accounting principles. Under those circumstances, regulatory assets or liabilities are recorded and such costs or credits are amortized over the periods they are included in rates in accordance with Statement of Financial Accounting Standards (SFAS) 71, "Accounting for the Effects of Certain Types of Regulation."

In order to defer incurred costs under SFAS 71, a regulated entity must have the statutory authority to establish rates that recover all costs and rates so established must be charged to and collected from customers. Due to increasing competitive pressures, BPA may be required to seek alternative solutions in the future to avoid raising rates to a level that is no longer competitive. If BPA's rates should become market-based, SFAS 71 would no longer be applicable, and any deferred costs and revenues under that standard would be expensed and recognized, respectively, in the Statement of Revenues and Expenses in that period. Amortization of these costs is reflected in the

Regulatory Assets and Liabilities

As of Sept. 30 — thousands of dollars

	2005	2004
Regulatory Assets		
Nonfederal projects:		
Conservation	**$ 40,264**	$ 43,566
Terminated hydro facilities	**27,305**	28,090
Terminated nuclear facilities	**3,917,450**	3,894,273
Decommissioning cost	**35,091**	52,059
IOU exchange benefits	**963,539**	988,259
Conservation	**298,189**	335,827
Fish and wildlife	**113,776**	116,910
Settlements	**51,592**	85,392
Federal Employee Compensation Act	**33,158**	—
Capital bond premiums	**22,632**	26,486
Additional post-retirement contributions	**6,600**	13,200
Total Regulatory Assets	**5,509,596**	5,584,062
Regulatory Liabilities		
Capitalization adjustment	**1,991,226**	2,056,131
Accumulated plant removal costs	**119,454**	105,270
Other	**18,980**	—
Total Regulatory Liabilities	**2,129,660**	2,161,401
Net Regulatory Assets and Liabilities	**$3,379,936**	$3,422,661

Statements of Revenues and Expenses. BPA does not earn a rate of return on its regulatory assets.

The previous table summarizes regulatory assets and liabilities as of Sept. 30, 2005, and 2004.

Federal Utility Plant

Federal utility plant is stated at original cost. Cost includes direct labor and materials; payments to contractors; indirect charges for engineering, supervision and similar overhead items; and an allowance for funds used during construction. The costs of additions, major replacements and betterments are capitalized. Repairs and minor replacements are charged to operating expense. The cost of federal utility plant retired is charged to accumulated depreciation when it is removed from service. The net cost of removal (the difference between cost of removal and salvage) is charged to the regulatory liability when cost of removal exceeds salvage. Federal utility plant in the Statements of Cash Flows is reported net of the accrued plant removal costs and accumulated depreciation.

Federal Projects Depreciation and Amortization

Depreciation of original cost and estimated cost to retire federal utility plant (i.e., net cost of removal) is computed on the straight-line method based on estimated service lives of the various classes of property, which average 40 years for transmission plant and 75 years for generation plant. Amortization of capitalized conservation and fish and wildlife costs is computed on the straight-line method based on estimated service lives, which are up to 20 years for conservation and 15 years for fish and wildlife.

Allowance for Funds Used During Construction

The allowance for funds used during construction (AFUDC) constitutes interest on the funds used for utility plant under construction. AFUDC is capitalized as part of the cost of utility plant and results in a non-cash reduction of interest expense. While cash is not realized currently from this allowance, it is realized under the ratemaking process over the service life of the related property through increased revenues resulting from higher plant in-service and higher depreciation expenses. AFUDC is based on the monthly construction work in progress balance.

AFUDC capitalization rates are stipulated in the congressional acts authorizing construction for Corps and Reclamation generating projects and were 2.1 percent to 4.9 percent in fiscal year 2005, 1.3 percent to 5.3 percent in fiscal year 2004, and 1.8 percent to 6.3 percent in fiscal year 2003.

AFUDC capitalization rates for BPA's construction projects were approximately 4.9 percent in fiscal year 2005, 5.3 percent in fiscal year 2004, and 6.3 percent in fiscal year 2003. These rates approximate the cost of borrowing from the U.S. Treasury.

Asset Retirement Obligations

SFAS 143, "Accounting for Retirement Obligations," requires the recognition of Asset Retirement Obligations (AROs), measured at estimated fair value, and for legal obligations related to the dismantlement and restoration costs associated with the retirement of tangible long-lived assets in the period in which the liability is incurred. Upon initial recognition of AROs that are measurable, the probability-weighted future cash flows for the associated retirement costs, discounted using a credit-adjusted risk-free rate, are recognized as a liability. Due to the long lead time involved, a market-risk premium cannot be determined for inclusion in future cash flows. FCRPS has certain tangible long-lived assets for which AROs are not measurable. An ARO will be required to be recorded when circumstances change. Assets that may require removal when no longer in service include the hydro projects and transmission facilities.

Pursuant to regulation, BPA recovers through rates estimated removal costs and records them as accumulated plant removal costs. At Sept. 30, 2005 and 2004, BPA has estimated these regulatory liabilities to be $119.5 million and $105.3 million, respectively.

Nonfederal Generation

BPA has acquired all of the generating capability of Energy Northwest's Columbia Generating Station (CGS) nuclear power plant. The contract to acquire the generating capability of the project, referred to as "a net-billing agreement," requires BPA to pay all or part of the annual project budget, including operating expense and debt service. BPA also has acquired all of the output of the Cowlitz Falls hydro project and agreed to pay the operating expense and debt service. BPA recognizes expenses for these projects based upon total project cash funding requirements. The nonfederal generation assets in the Balance Sheets are amortized as the principal on the outstanding bonds is repaid. See Note 4 Nonfederal Projects and Related Debt.

Cash

For purposes of reporting cash flows, amounts include cash in the BPA fund and unexpended appropriations of the Corps and Reclamation. Cash paid for interest on appropriated funds and bonds issued to U.S. Treasury was $78 million, $102 million and $135 million in fiscal years 2005, 2004, and 2003, respectively. These amounts are net of U.S. Treasury credits and interest income earned on the Bonneville fund.

Financial Instruments

All significant financial instruments of the FCRPS were recognized in the Balance Sheets as of Sept. 30, 2005 and 2004. The carrying value reflected in the Balance Sheets approximates fair value for the FCRPS' financial assets and current liabilities. The fair values of bonds issued to U.S. Treasury and nonfederal projects are discussed in Notes 3 and 4 for Bonds issued to U.S. Treasury and Nonfederal Projects and Related Debt, respectively.

Concentrations of Credit Risks

General Credit Risk

Financial instruments, which potentially subject the FCRPS to concentrations of credit risk, consist primarily of BPA accounts receivable. Credit risk represents the loss that would be recognized if counterparties fail to perform as contracted.

BPA's accounts receivables are spread across a diverse group of public utilities, investor-owned utilities, power marketers, and others that are geographically located throughout the Western United States and Canada. The accounts receivable exposures result from BPA providing a wide variety of power products and transmission services. BPA's counterparties are generally large and stable and do not represent a significant concentration of credit risk. During fiscal year 2005, BPA experienced no significant losses as a result of any customer defaults or bankruptcy filings.

Credit risk is mitigated at BPA by reviewing counterparties for creditworthiness, establishing credit limits, and monitoring credit exposure on a daily basis, and performing Credit Value at Risk (CVaR) measurements for forward power transactions on a weekly basis. In order to further manage credit risk, BPA obtains credit support such as letters of credit and third-party guarantees from some counterparties. Counterparties are monitored closely for changes in financial condition and credit reviews are updated regularly.

Allowance for Doubtful Accounts

Management reviews accounts receivable on a monthly basis to determine if any receivable will potentially be uncollectible. The allowance for doubtful accounts includes amounts estimated through an evaluation of specific accounts, based upon the best available facts and circumstances, of customers that may be unable to meet their financial obligations, and a reserve based on historical experience. Management believes that the allowance for doubtful accounts as of Sept. 30, 2005, was adequate.

Credit Risk from California

California power markets were in turmoil several years ago and experienced historically high power prices and volatility along with the continued uncertainty related to deregulation. The California Independent System Operator and California Power Exchange, two customers with whom BPA had contracts for power and transmission delivery during that period have been unable to fully pay BPA for their purchases. BPA has recorded an allowance for doubtful accounts which in management's best estimate are sufficient to cover potential exposure. Net exposure after the allowance is not significant. Nonetheless, BPA is continuing to pursue collection of amounts due in bankruptcy and other proceedings.

Deferred Charges and Other

SFAS 133 derivative mark-to-market represents unrealized fair value gains of derivative contracts. The NIFC trust fund is held for construction of the Schultz-Wautoma transmission line. Energy receivable is energy to be returned to BPA for prior transmission line losses.

Deferred Charges and Other

As of Sept. 30 — thousands of dollars

	2005	2004
SFAS 133 derivative mark-to-market	**$175,591**	$172,713
NIFC trust fund	**26,731**	31,194
Energy receivable	**18,980**	—
Other	**13,471**	60,112
	$234,773	$264,019

Other is primarily Corps and Reclamation costs for generating assets not placed in service. The Corps disposed of generating units related to the Libby Dam of $40 million in fiscal year 2005.

The previous table summarizes deferred charges and other as of Sept. 30, 2005 and 2004.

Retirement Benefits

FCRPS employees are participants in either the Civil Service Retirement System (CSRS) or the Federal Employees Retirement System (FERS). Both FCRPS and its employees contribute a percentage of eligible employee compensation toward funding these defined post-retirement benefit plans. Based on the statutory contribution rates, retirement benefit expense under CSRS is equivalent to 7 percent of eligible employee compensation and under FERS is equivalent to 11.2 percent of eligible employee compensation. However, the legislatively mandated contribution levels do not fully cover the cost to the federal government to provide the plan benefits. Therefore, the programs are considered under funded. Employees also may be participants in the Federal Employees Health Benefits Program (FEHB) and/or the Federal Employees' Group Life Insurance Program (FEGLI); these plans are similarly under funded. Retirement benefits are payable by the U.S. Treasury and not by the FCRPS.

In order to ensure that all post-retirement benefit programs provided to its employees are fully funded and such costs are both recovered through rates and properly expensed, FCRPS makes additional annual contributions to the U.S. Treasury. Because these costs are included in rates, the deferred amount has been recorded as a regulatory asset. FCRPS has a $6.6 million remaining liability as of Sept. 30, 2005, which is included in other current liabilities and deferred credits in the accompanying Balance Sheet representing the balance of deferred additional contributions from fiscal years 1998 through 2001. The liability is reduced as prior years' additional contributions are made. FCRPS expects to satisfy its prior year commitments for under funded post-retirement benefits by fiscal year 2007.

Deferred Credits

Revenues associated with advances for customer reimbursable projects are recognized in two different ways. If the customer will own the asset under construction, the revenue is recognized as the expenditures are incurred. If BPA will own the resulting asset, revenue is recognized over the life of the asset, once the corresponding asset is placed in service.

Deferred revenues for Third AC intertie capacity agreements are recognized over an estimated 49-year life of the related assets.

Load diversification fees are payments or settlements by customers to BPA in consideration for a reduction in their contractually obligated power purchases from BPA. Deferred load diversification fees and other settlement payments for long-term agreements are recognized as revenue over the original contract terms (load diversification fee contracts generally correspond to the rate period ended Sept. 30, 2001, while other settlement agreements extend over varying periods through 2019).

Up-front leasing fees for fiber optic cable are recognized over the lease terms extending as far as 2020.

The Federal Employees Compensation Act (FECA) authorizes income and medical cost protection to covered federal civilian employees that are injured on the job or that have incurred a work-related injury or occupational disease. The U.S. Department of Labor (DOL) administers compensation and medical benefits paid under FECA on behalf of the Federal Government. DOL is also responsible for calculating the FECA liability of future compensation benefits for all federal agencies. FCRPS records its respective portion of the actuarial liability for the estimated amount of future payment for workers' compensation benefits as a liability on its fiscal year 2005 Balance Sheet. This actuarial liability includes the expected liability for death, disability, medical and miscellaneous costs for approved compensation cases plus a component for incurred but not reported claims.

SFAS 133 derivative mark-to-market represents fair value of derivatives.

The table below summarizes deferred credits as of Sept. 30, 2005 and 2004.

Deferred Credits

As of Sept. 30 — thousands of dollars

	2005	2004
Customer reimbursable projects	**$ 177,419**	$183,933
Third AC intertie capacity agreements	**116,481**	119,546
Load diversification fees	**71,617**	81,163
Fiber optic leasing fees	**55,444**	59,335
Federal Employee Compensation Act	**33,158**	—
SFAS 133 derivative mark-to-market	**16,329**	106,513
Other	**11,636**	64,212
	$ 482,084	$614,702

SFAS 133 and Related Guidance

SFAS 133, "Accounting for Derivative Instrument and Hedging Activities," requires that every derivative instrument be recorded on the balance sheet as an asset or liability measured at its fair value and that change in the derivative's fair value be recognized currently in earnings unless specific hedge accounting criteria are met.

It is BPA's policy to document and apply as appropriate the normal purchase and normal sales exception under SFAS 133, as amended by SFAS 138, "Accounting for Certain Derivative Instruments and Certain Hedging Activities," related Derivative Implementation Group (DIG) guidance, and SFAS 149, "Amendment of Statement 133 on Derivative Instruments and Hedging Activities." Collectively, these statements are referred to as "SFAS 133." Purchases and sales of forward electricity and option contracts that require physical delivery and which are expected to be used or sold by the reporting entity in the normal course of business are generally considered "normal purchases and normal sales" under SFAS 133. These transactions are not required to be recorded at fair value in the financial statements.

For all other derivative transactions BPA applies fair value accounting and records the amounts in the current period Statement of Revenues and Expenses. BPA does not apply hedge accounting.

BPA recorded a SFAS 133 mark-to-market unrealized gain in the Statement of Revenues and Expenses related to its derivative portfolio (including physical power purchase and sale transactions, power exchange transactions, and purchased options) of $94.6 million, $89.4 million and $55.3 million for fiscal years 2005, 2004 and 2003, respectively.

Purchased Options

In fiscal years 2005 and 2004, BPA purchased physical put options for the right to sell electricity at certain points in the future. With significant inventory risk due to currently unpredictable annual runoff, the put options allow BPA to hedge against falling prices without committing inventory and increasing the inventory risk.

BPA records purchased options on a mark-to-market basis and includes unrealized gains and losses in operating revenues in the Statement of Revenues and Expenses.

Interest Rate Swap Transactions

In fiscal year 2003, BPA entered into two floating-to-fixed LIBOR interest rate swaps to help manage interest rate risk related to its long-term debt portfolio. In the first swap transaction, BPA pays a fixed 3.1 percent on $300 million notional amount for 10 years and receives a variable rate that changes weekly tied to LIBOR. In the second swap transaction, BPA pays a fixed 3.5 percent on $200 million notional amount for 15 years and receives a variable rate that changes weekly tied to LIBOR. The floating interest rates on the swaps are reset on a weekly basis. The net effect of the two swap transactions is essentially replacing variable rate debt with 3.3 percent fixed rate debt. The swap transactions do not qualify for hedge accounting treatment under SFAS 133. BPA recorded a $4.3 million unrealized fair value gain, a $2.1 million unrealized fair value gain and a $7.9 million unrealized fair value loss in the Statements of Revenues and Expenses for fiscal years 2005, 2004 and 2003 respectively, related to the interest rate swap transactions.

EITF 03-11

Emerging Issues Task Force Issue No. 03-11 (EITF 03-11), "Reporting Realized Gains and Losses on Derivative Instruments that are Subject to FASB Statement No. 133, Accounting for Derivative Instruments and Hedging Activities, and Not Held for Trading Purposes," requires that revenues and expenses associated with non-trading energy activities that are "booked out" (not physically settled) be reported on a net basis. EITF 03-11 is effective for all derivative contracts that settle after Sept. 30, 2003, and does not require the reclassification of prior period amounts. Effective with the Oct. 1, 2003 adoption of EITF 03-11, the non-physical settlement of non-trading electricity derivative activities, formerly recorded on a "gross" basis in both operating revenues and purchased power expense, are now recorded on a "net" basis in operating revenues. This change, which has no effect on margins, net revenue or cash flows, resulted in a $239 million and $212 million decrease to both operating revenues and purchased power expense for fiscal years 2005, and 2004, respectively. The determination of the sales and purchases of electricity that would have been reported on a net basis had EITF 03-11 been historically applied is not practicable. Prospective application of EITF 03-11 will continue to result in a significant decrease in reported non-trading wholesale energy sales and purchases and related amounts reported in comparative financial statements.

Revenues and Net Revenues

Operating revenues are recorded on the basis of service rendered, which includes estimated unbilled revenues of $209 million, $158 million and $190 million at Sept. 30, 2005, 2004 and 2003, respectively. For revenue purposes, BPA operates as two segments: the Power Business Line and the Transmission Business Line. In Note 8 Segments, the table reflects revenues and expenses attributable to each business line. Because BPA is a U.S. government power marketing administration, net revenues over time are committed to repayment of the U.S. government investment in the FCRPS and the payment of certain irrigation costs as discussed in Note 7 Commitments and Contingencies.

U.S. Treasury Credits for Fish

The Northwest Power Act of 1980 obligated the BPA administrator to make expenditures for fish and wildlife protection, mitigation and enhancement for both power and non-power purposes, on a reimbursement basis. The Northwest Power Act also specified that consumers of electric power, through their rates for power services "shall bear the costs of measures designed to deal with adverse impacts caused by the development and operation of electric power facilities and programs only." Section 4(h)(10)(C) of the Northwest Power Act was designed to ensure that the costs of mitigating these impacts are properly accounted for among the various purposes of the hydroelectric projects. In the early 1990s, BPA, the U.S. Treasury and the Office of Management and Budget agreed to a crediting mechanism whereby BPA reduces its cash payments to the U.S. Treasury by an amount equal to the mitigation measures funded on behalf of the non-power purposes. BPA has taken U.S. Treasury credits for fish annually since 1995.

Recent Accounting Pronouncements

In December 2004, the FASB issued SFAS No. 153, "Exchanges of Nonmonetary Assets – An Amendment of APB Opinion No. 29, Accounting for Nonmonetary Transactions," which redefines the types of non-monetary exchanges that require fair value measurement. SFAS No. 153 is effective for nonmonetary exchanges made in fiscal years beginning after June 15, 2005. Adoption of this new standard in fiscal year 2006 is not expected to have a material impact on BPA's financial condition, results of operations or cash flows.

In March 2005, the FASB issued FASB Interpretation No. (FIN) 47, "Accounting for Conditional Asset Retirement Obligations, an interpretation of FASB Statement No. 143." FIN 47 clarifies that an entity is required to recognize a liability for a legal obligation to perform an asset retirement activity if the fair value can be reasonably estimated even though the timing and (or) method of settlement are conditional on a future event. FIN 47 is effective no later than the end of fiscal years ending after Dec. 15, 2005; therefore, it would be applicable no later than the end of BPA's fiscal year 2006. BPA is evaluating the effect of the adoption and implementation of FIN 47. Adoption of this guidance is not expected to have a material impact on BPA's financial condition, results of operations or cash flows.

2. Federal Appropriations

The BPA Appropriations Refinancing Act (Refinancing Act), 16 U.S.C. 8381, required that the outstanding balance of the FCRPS federal appropriations, which BPA is obligated to set rates to recover, be reset and assigned prevailing market rates of interest as of Sept. 30, 1996. The resulting principal amount of appropriations was determined to be equal to the present value of the principal and interest that would have been paid to the U.S. Treasury in the absence of the Refinancing Act, plus $100 million. The $100 million was capitalized as part of the appropriations balance and was included pro rata in the new principal of the individual appropriated repayment obligations. The amount of appropriations refinanced was $6.6 billion. After refinancing, the appropriations outstanding were $4.1 billion. The difference between the appropriated debt before and after the refinancing was recorded as a capitalization adjustment in regulatory liabilities. This adjustment is being amortized over the remaining period of repayment so that total FCRPS net interest expense is equal to what it would have been in the absence of the Refinancing Act. Amortization of the capitalization adjustment was $64.9 million, $68.6 million and $67.7 million for fiscal years 2005, 2004 and 2003, respectively.

Construction and replacement of Corps and Reclamation generating facilities historically have been financed through annual federal appropriations. Annual appropriations also were made for their operation and maintenance costs, although these are normally repaid by BPA to the U.S. Treasury by the end of each fiscal year. The Energy Policy Act of 1992 authorized BPA to directly fund operation and maintenance expenses and capital efficiency and reliability improvements for Corps and Reclamation generating facilities.

Federal generation and transmission appropriations are repaid to the U.S. Treasury within the weighted average service lives of the associated investments (maximum 50 years) from the time each facility is placed in service.

If, in any given year, revenues are not sufficient to cover all cash needs, including interest, any deficiency becomes an unpaid annual expense. Interest is accrued on the unpaid annual expense until paid. This interest must be paid from subsequent years' revenues before any repayment of federal appropriations can be made.

The following table shows the term repayments on the remaining federal appropriations as of Sept. 30, 2005.

Federal Appropriations

As of sept. 30 — thousands of dollars

Term Repayments	
2006	$ 68,939
2007	33,694
2008	10,913
2009	9,889
2010	26,327
2011+	4,191,839
	$ 4,341,601

Includes payments on historic replacements but excludes planned future replacements and irrigation assistance.

The weighted average interest rate was 6.7 percent on outstanding appropriations as of Sept. 30, 2005.

3. Bonds issued to U.S. Treasury

To finance its capital programs, BPA is authorized by Congress to issue to the U.S. Treasury up to $4.45 billion of interest-bearing debt with terms and conditions comparable to debt issued by U.S. government corporations. Of the $4.45 billion, $1.25 billion is reserved for conservation and renewable resource loans and grants. At Sept. 30, 2005, of the total $2.78 billion of outstanding bonds, $779.8 million were conservation and renewable resource loans and grants (including Corps, Reclamation and U.S. Fish & Wildlife capital investments). The average interest rate of BPA's borrowings from the U.S. Treasury exceeds the rate that could be obtained currently. As a result, the fair value of BPA bonds issued to U.S. Treasury, based upon discounting future cash flows using rates offered by the U.S. Treasury as of Sept. 30, 2005, for similar maturities, exceeds carrying value by approximately $169 million, or 6.1 percent.

The following table reflects the terms and amounts of bonds issued to U.S. Treasury.

Bonds issued to U.S. Treasury

Long-Term Debt — thousands of dollars

	First Call Date	Maturity Date	Interest Rate	Amount	Cumulative Total
October 2002	none	2005	3.00%	$ 50,000	$ 50,000
November 2002	none	2005	2.80%	40,000	90,000
April 2003	none	2006	2.40%	40,000	130,000
April 2003	none	2006	2.40%	25,000	155,000
July 2003	none	2006	2.30%	75,000	230,000
July 2003	none	2006	2.30%	30,000	260,000
August 1996	none	2006	7.05%	70,000	330,000
September 2000	none	2006	6.75%	40,000	370,000
September 2002	none	2006	3.05%	100,000	470,000
September 2002	none	2006	3.05%	30,000	500,000
September 2002	none	2006	3.05%	20,000	520,000
September 2003	none	2006	2.50%	20,000	540,000
September 2003	none	2006	2.50%	25,000	565,000
December 2002	none	2006	3.05%	40,000	605,000
January 2004	none	2007	2.50%	60,000	665,000
January 2004	none	2007	2.50%	25,000	690,000
April 2003	none	2007	2.90%	40,000	730,000
April 2004	none	2007	2.95%	65,000	795,000
April 2004	none	2007	2.95%	35,000	830,000
July 2003	none	2007	2.95%	25,000	855,000
July 2004	none	2007	3.45%	50,000	905,000
July 2004	none	2007	3.45%	25,000	930,000
August 1997	none	2007	6.65%	111,300	1,041,300
September 2003	none	2007	3.10%	20,000	1,061,300
September 2004	none	2007	3.10%	30,000	1,091,300
September 2004	none	2007	3.10%	30,000	1,121,300
November 2004	none	2007	3.50%	20,000	1,141,300
January 2004	none	2008	2.95%	65,000	1,206,300
January 2004	none	2008	2.95%	30,000	1,236,300
January 2005	none	2008	3.60%	20,000	1,256,300

	First Call Date	Maturity Date	Interest Rate	Amount	Cumulative Total
April 1998	none	2008	6.00%	75,300	$1,331,600
April 1998	none	2008	6.00%	25,000	1,356,600
June 2005	none	2008	3.95%	30,000	1,386,600
July 2004	none	2008	3.80%	25,000	1,411,600
August 1998	none	2008	5.75%	40,000	1,451,600
September 1998	none	2008	5.30%	104,300	1,555,900
September 2005	none	2008	4.25%	25,000	1,580,900
September 2005	none	2008	4.25%	20,000	1,600,900
November 2004	none	2008	3.75%	35,000	1,635,900
May 1998	none	2009	6.00%	72,700	1,708,600
May 1998	none	2009	6.00%	37,700	1,746,300
June 2005	none	2009	4.00%	40,000	1,786,300
July 1989	none	2009	8.55%	40,000	1,826,300
January 2001	none	2010	6.05%	60,000	1,886,300
January 2001	none	2010	6.05%	30,000	1,916,300
May 1998	none	2011	6.20%	40,000	1,956,300
June 2001	none	2011	5.95%	25,000	1,981,300
August 2001	none	2011	5.75%	50,000	2,031,300
January 1998	none	2013	6.10%	60,000	2,091,300
September 1998	none	2013	5.60%	52,800	2,144,100
February 1999	none	2014	5.90%	60,000	2,204,100
April 1998	2008	2028	6.65%	50,000	2,254,100
August 1998	none	2028	5.85%	106,500	2,360,600
August 1998	none	2028	5.85%	112,300	2,472,900
May 1998	2008	2032	6.70%	98,900	2,571,800
April 2003	2008	2033	5.55%	40,000	2,611,800
September 2004	2009	2034	5.60%	40,000	2,651,800
January 2005	2010	2035	5.40%	40,000	2,691,800
April 2005	2010	2035	5.50%	40,000	2,731,800
September 2005	2010	2035	5.25%	45,000	2,776,800
				$2,776,800	$2,776,800
Less current portion					(565,000)
					$2,211,800

All construction, conservation, fish and wildlife, and Corps/Reclamation direct funding bonds are term bonds.

The weighted average interest rate was 4.8 percent on outstanding bonds issued to U.S. Treasury as of Sept. 30, 2005.

4. Nonfederal Projects and Related Debt

In addition to the CGS nuclear generating project, BPA has also acquired all or part of the generating capability of four other nuclear projects which are not providing power. These other projects are Energy Northwest Nuclear Project No. 1 (Project 1), Nuclear Project No. 3 (Project 3), 72 percent of the Hanford Generating Plant, and 30 percent of the Trojan project owned by Eugene Water and Electric Board (EWEB), Portland General Electric and PacifiCorp. The contracts to acquire the generating capability of the non-operating nuclear projects are also "net-billing agreements" requiring BPA to pay all or part of the annual projects' budgets, including maintenance expense and debt service. Project 1 and Project 3 were terminated prior to completion. Hanford and Trojan were decommissioned.

Along with the Cowlitz Falls hydro generating project, BPA has acquired all of the generating capability of Northern Wasco hydro project and agreed to pay the maintenance expense and debt service. However, the project was terminated prior to completion.

BPA has agreed to fund debt service on Emerald People's Utility District loans, Conservation and Renewable Energy System and City of Tacoma Conservation bonds, all issued to finance conservation programs sponsored by BPA.

Operating projects are included in nonfederal generation and non-operating projects are included in regulatory assets. See Note 1 Summary of Significant Accounting Policies. The debt for both the operating and non-operating nonfederal projects is included in nonfederal projects debt. BPA recognizes expenses for these projects based upon total project cash funding requirements.

Operating and maintenance expense for the projects of $257 million, $235 million and $223 million in fiscal years 2005, 2004 and 2003, respectively, is included in operations and maintenance in the accompanying Statements of Revenues and Expenses. Debt service for the projects of $292 million, $248 million, and $120 million for fiscal years 2005, 2004 and 2003, respectively, is reflected as nonfederal projects expense in the accompanying Statements of Revenues and Expenses.

The fair value of all Energy Northwest debt exceeds recorded value by $116 million, or 1.9 percent based on discounting the future cash flows using interest rates for which similar debt could be issued at Sept. 30, 2005. All other nonfederal projects' debt approximates fair value as stated.

Construction of the Schultz-Wautoma transmission line was financed through NIFC. In March 2004, NIFC issued $119.6 million in taxable bonds to finance the line under a lease-purchase agreement. NIFC owns the line and BPA leases the line for 30 years. Lease revenues from BPA back the bonds.

BPA is constructing and will operate the line. BPA has indemnified the equity owners of NIFC for all construction and operating risks associated with the line. BPA will have exclusive use and control of the asset during the lease period. At the end of the lease, BPA has the option to buy the line for ten dollars. BPA has determined it is the primary beneficiary of NIFC. As such, NIFC financial statements are consolidated into BPA financial statements in accordance with FIN 46. The bonds are included as nonfederal debt on FCRPS' financial statements. NIFC's assets are included in FCRPS' other assets at Sept. 30, 2005. The following table summarizes future nonfederal projects principal payments as of Sept. 30, 2005.

Nonfederal Projects Debt

As of Sept. 30 — thousands of dollars

	Principal Payments
2006	$ 207,491
2007	295,350
2008	306,958
2009	311,294
2010	362,860
2011+	5,010,096
	$ 6,494,049

The weighted average interest rate was 5.5 percent on the major portion of outstanding nonfederal projects debt as of Sept. 30, 2005.

5. Nonfederal Nuclear AROs

The AROs for CGS, Project 1, and Trojan are $160.6 million and $164 million at Sept. 30, 2005 and 2004, respectively. BPA has funded $125.5 million for these AROs, which is held in trusts and recorded in the Balance Sheet. The trust fund balances are $95 million and $30.5 million for decommissioning and site restoration, respectively at Sept. 30, 2005. Payments to the trusts for fiscal years 2005, 2004 and 2003 were approximately $5.5 million, $5 million and $4.8 million, respectively. The unfunded amount will be collected in future rates and is included in regulatory assets in the Balance Sheet.

The following table presents the effects to the balances and activities in AROs for the accounting periods reported herein. Revisions were made in the current and prior years adjusting the accretion rates from the original model and calculation.

Nonfederal Nuclear AROs Activity

For the years ended Sept. 30 — thousands of dollars

	2005	2004	2003
Beginning Balance	**$164,000**	$126,000	$129,900
Activity:			
Expenditures	**(7,800)**	(7,900)	(7,000)
Accretion	**7,700**	6,800	3,100
Revisions	**(3,300)**	39,100	—
Ending Balance	**$160,600**	$164,000	$126,000

Decommissioning costs for CGS are charged to operations over the operating life of the project. An external decommissioning trust fund for costs is being funded monthly for CGS. The trust funds are expected to provide for decommissioning at the end of the project's safe storage period in accordance with Nuclear Regulatory Commission (NRC) requirements. The NRC requires that this deferred decontamination period be no longer than 60 years. Trust fund requirements for CGS are based on a NRC decommissioning cost estimate and assume a 40-year operating life.

The estimated decommissioning and site restoration expenditures for CGS are $673 million (2003 dollars). BPA has recorded an estimated liability of $98.2 million, $49.1 million and $13.3 million on a fair value basis for CGS and Trojan decommissioning costs, and Project 1 site restoration, respectively.

In fiscal years 2004 and 2005, BPA directly funded Trojan decommissioning expenses. BPA will continue to recover EWEB's 30 percent share of Trojan's costs through rates. Decommissioning costs are included in operations and maintenance expense in the accompanying Statements of Revenues and Expenses. These costs incorporate the impact of SFAS 143.

6. Investor-owned Utility Exchange Benefits

As provided for in the Northwest Power Act, beginning in 1982 BPA entered into residential exchange contracts with most of its electric utility customers. These contracts resulted in payments to the utilities if a utility's average system cost exceeded BPA's priority firm power rate on the "exchanged" power. These payments were required to be passed through to their qualified residential and small-farm customers.

Subsequently, contract termination agreements were signed by all actively exchanging Pacific Northwest utilities except Northwestern Energy (formerly the Montana Power Co.), which had not been receiving benefits. BPA made payments to settle the utilities' and BPA's rights and obligations under the residential exchange program through June 30, 2001, and in some cases, through June 30, 2011.

In October 2000, BPA's investor-owned utility (IOU) customers signed Subscription settlement agreements, under which BPA was to provide monetary and power benefits in place of residential exchange benefits for the period July 1, 2001, through Sept. 30, 2011. These agreements provide for both sales of power and monetary benefit payments to the IOUs and also allow the power to be converted to cash payments.

Amendments to the October 2000 contracts allowed payment of a portion of the fiscal year 2003 IOU Subscription settlement benefits to be deferred and paid in the fiscal year 2007 through 2011 period, except when they were reduced through credits to offset the SN CRAC.

In May 2004, BPA signed new contracts and amendments with all six IOU customers entitled "Agreements Regarding Payment of Residential Exchange Program Settlement Benefits During Fiscal Years 2007-2011." These latest agreements established a method for calculating the IOUs' Monetary Benefits for the fiscal years 2007 through 2011 period including an annual floor of $100 million and an annual cap of $300 million for the six IOUs in total, and all parties agreed that BPA would have no obligation to provide power to the IOUs during that period. The new agreements also eliminated $100 million of a $200 million risk contingency payment owed to two IOUs that have load reduction payments, and deferred the remaining $100 million payment and related interest to the fiscal years 2007 through 2011 period.

IOU Exchange Benefit amounts for the fiscal year 2007 through 2011 period cannot yet be calculated; however, the annual floor of $100 million has been recorded as a liability totaling $500 million. In addition, the IOU Risk Contingency Payment amounts that were deferred in fiscal year 2004 will be repaid $20 million per year (plus interest) during the fiscal year 2007 through 2011 period and have been recorded as a liability. The IOU Exchange Benefits recorded on the Balance Sheet at Sept. 30, 2005 includes $357 million for fiscal year 2006. The amounts to be collected through future rates are included in regulatory assets.

Further, it is possible that these agreements may be revised in connection with legal challenges that have been filed with the Ninth Circuit Court, which could result in a remand and potential changes to the IOU Exchange Benefit Amounts to be provided to the IOU customers. BPA believes it is likely that the agreements will be sustained and, as such, the annual floor.

7. Commitments and Contingencies

Purchase and Sales Commitments

Subscription contracts are the basis for the contractual relationship between BPA and nearly all of its firm power customers. BPA has entered into Subscription power sales for 3,000 average megawatts more power than the federal system produces on a firm-planning basis. These contracts run for as short as three years and as long as 10 years from Oct. 1, 2001. Current rates recover the additional costs of the Subscription obligations through fiscal year 2006. BPA's trading floor enters into sales commitments to sell expected surplus generating capabilities at future dates and purchase commitments to purchase power at future dates when BPA forecasts a shortage of generating capability and prices are favorable. Further, BPA enters into these contracts throughout the year to maximize its revenues on estimated surplus volumes. BPA records these sales and purchases in the month the underlying power is delivered.

The table below summarizes future purchase power and sales commitments as of Sept. 30, 2005.

Purchase Power and Sales Commitments

As of Sept. 30 — thousands of dollars

	Purchase	Sales
2006	$ 559,067	$ 2,095,743
2007	19,472	1,711,918
2008	18,847	1,723,573
2009	53,102	1,722,475
2010	53,102	1,806,711
2011	54,027	1,802,767
	$757,617	**$10,863,187**

Augmentation commitments run through 2006. Purchases and sales have not been adjusted for EITF 03-11 net basis reporting.

Irrigation Assistance

As directed by legislation, BPA is required to make cash distributions to the U.S. Treasury for original construction costs of certain Pacific Northwest irrigation projects that have been determined to be beyond the irrigators' ability to pay. These irrigation distributions do not specifically relate to power generation and are required only if doing so does not result in an increase to power rates. Accordingly, these distributions are not considered to be regular operating costs of the power program and are treated as distributions from accumulated net revenues (expenses) when paid. BPA paid irrigation assistance payments of $739 thousand in fiscal year 2004. Future irrigation assistance payments ultimately could total $667 million and are scheduled over a maximum of 66 years. BPA is required by Public Law 89-448 to demonstrate that reimbursable costs of the FCRPS will be returned to the U.S. Treasury from BPA net revenues within the period prescribed by law. BPA is required to make a similar demonstration for the costs of irrigation projects, which are beyond the ability of the 22 irrigation water users to repay. These requirements are met by conducting power repayment studies including schedules of distributions at the proposed rates to demonstrate repayment of principal within the allowable repayment period.

The following table summarizes future irrigation assistance distributions as of Sept. 30, 2005.

Irrigation Assistance

As of Sept. 30 — thousands of dollars

Scheduled Distributions

2006	$ —
2007	—
2008	2,950
2009	6,590
2010	—
2011+	657,693
	$667,233

Excludes $56.6 million for Lower Teton, which was never completed, therefore never produced electricity and the administrator has no obligation to recover these costs.

Additional Post-Retirement Contributions

FCRPS makes additional annual contributions to the U.S. Treasury in order to ensure that all federal post-retirement benefit programs provided to its employees are fully funded and such costs are both recovered through rates and properly expensed. The additional contributions are based on employee plan participation and the extent to which the particular plans are under funded. BPA paid $26.5 million, $30.9 million and $35.1 million to the U.S. Treasury during fiscal years 2005, 2004 and 2003, respectively. These amounts were recorded as expense when paid. At Sept. 30, 2005, FCRPS has scheduled additional payments totaling $124 million as shown in the following table.

Additional Post-Retirement Contributions

As of Sept. 30 — thousands of dollars

Scheduled Contributions

2006	$ 23,200
2007	21,100
2008	18,000
2009*	30,554
2010*	31,195
	$ 124,049

FCRPS expects to recognize these amounts as expense in the years in which they are specifically recovered through rates.

* Estimates not currently scheduled.

Net-Billing Agreements

BPA has agreed with Energy Northwest that in the event any participant shall be unable for any reason, or shall refuse, to pay to Energy Northwest any amount due from such participant under its net-billing agreement for which a net-billing credit or cash payment to such participant has been provided by BPA,

BPA will be obligated to pay the unpaid amount in cash directly to Energy Northwest, unless payment of such unpaid amount is made in a timely manner pursuant to the net-billing agreements.

Nuclear Insurance

BPA is a member of the Nuclear Electric Insurance Limited (NEIL), a mutual insurance company established to provide insurance coverage for nuclear power plants. The types of insurance coverage purchased from NEIL by BPA include: 1) Primary Property and Decontamination Liability Insurance; 2) Decommissioning Liability and Excess Property Insurance; and 3) Business Interruption and/or Extra Expense Insurance.

Under each insurance policy BPA could be subject to an assessment in the event that a member-insured loss exceeds reinsurance and reserves held by NEIL. The maximum assessment for the Primary Property and Decontamination Insurance policy is $6.8 million. For the Decontamination Liability, Decommissioning Liability and Excess Property Insurance policy, the maximum assessment is $14.1 million. For the Business Interruption and/or Extra Expense Insurance policy, the maximum assessment is $4.5 million.

As a separate requirement, BPA is liable under the Nuclear Regulatory Commission's indemnity for public liability coverage under the Price-Anderson Act. In the event of a nuclear accident resulting in public liability losses exceeding $300 million, BPA could be subject to a retrospective assessment of up to $95.8 million limited to an annual maximum of $10 million. Assessments would be included in BPA's costs and recovered through rates.

Environmental Matters

From time to time, there are sites for which BPA, Corps or Reclamation has been or may be identified as a potential responsible party. Costs associated with cleanup of those sites are not expected to be material to the FCRPS' financial statements and would be recoverable through rates.

Litigation

In the fall of 2002, two separate groups of BPA customers filed separate petitions with the Ninth Circuit Court relating to the contracts for the Slice Product (Slice Agreements). These petitions have been consolidated into a single proceeding along with a third petition filed in 2004. Under the Slice Agreements, BPA is to determine certain after-the-fact annual adjustments to the Slice power rate to reflect actual costs (True-up Charges). The principal petition was filed by Slice customers seeking to reverse $84 million in BPA-determined True-up Charges for fiscal year 2002. The Slice customer litigants assert that BPA's determination of the charges is not consistent with the Slice Agreements and that the Slice Agreements require binding arbitration of such disputes such that the Ninth Circuit Court lacks jurisdiction to resolve the correctness of BPA's determination of the charges. BPA and the other litigants are attempting to resolve the dispute through mediation while the litigation moves forward. BPA continues to maintain that the charges are consistent with the Slice Agreements. Depending on the result of the mediation, or alternatively the litigation pertaining to the 2002 True-up Charges, it is possible that True-up Charges with respect to fiscal years 2003 and thereafter could be adjusted.

The FCRPS is party to various other legal claims, actions and complaints, certain of which involve material amounts. Although the FCRPS is unable to predict with certainty whether or not it will ultimately be successful in these legal proceedings or, if not, what the impact might be, management currently believes that disposition of these matters will not have a materially adverse effect on the FCRPS' financial position or results of operations.

Judgments and settlements are included in BPA's costs and recovered through rates.

8. Segments

BPA follows FERC's open-access rulemaking and standards of conduct. FERC requires that transmission activities are functionally separate from wholesale power merchant functions and that transmission is provided in a nondiscriminatory open-access manner.

The FCRPS' major operating segments are defined by the utility functions of generation and transmission. In the following table, the Power Business Line represents the operations of the generation function, while the Transmission Business Line represents the operations of the transmission function. The business lines are not separate legal entities. "Other" represents items that are necessary to reconcile to the financial statements. These items generally include shared activity such as debt management actions and inter-business unit eliminations. Each FCRPS segment operates predominantly in one industry and geographic region: the generation and transmission of electric power in the Pacific Northwest.

The FCRPS centrally manages all interest expense activity. Since BPA has one fund with the U.S. Treasury, all cash and cash transactions are also centrally managed. Unaffiliated revenues represent sales to external customers for each segment. Inter-segment revenues are eliminated.

During fiscal years 2005, 2004 and 2003, no single customer represented 10 percent or more of the FCRPS' revenues.

Segment Reporting

For the years ended Sept. 30 — thousands of dollars

	Power	Transmission	Other	FCRPS
2005				
Unaffiliated revenues	**$ 2,740,700**	**$ 527,383**	**$ —**	**$3,268,083**
Intersegment revenues	**73,524**	**107,147**	**(180,671)**	**—**
Total operating revenues	**2,814,224**	**634,530**	**(180,671)**	**3,268,083**
Unaffiliated expenses	**2,025,938**	**260,060**	**(157,669)**	**2,128,329**
Depreciation	**186,099**	**189,501**	**—**	**375,600**
Intersegment expenses	**106,510**	**73,524**	**(180,034)**	**—**
Total operating expenses	**2,318,547**	**523,085**	**(337,703)**	**2,503,929**
Net operating revenues	**495,677**	**111,445**	**157,032**	**764,154**
Interest expense	**166,610**	**135,754**	**(25,080)**	**277,284**
Net revenues (expenses)	**$ 329,067**	**$ (24,309)**	**$ 182,112**	**$ 486,870**
2004				
Unaffiliated revenues	$ 2,661,975	$ 535,936	$ —	$3,197,911
Intersegment revenues	76,923	108,123	(185,046)	—
Total operating revenues	2,738,898	644,059	(185,046)	3,197,911
Unaffiliated expenses	1,971,620	252,738	(181,952)	2,042,406
Depreciation	177,297	188,942	—	366,239
Intersegment expenses	108,194	76,758	(184,952)	—
Total operating expenses	2,257,111	518,438	(366,904)	2,408,645
Net operating revenues	481,787	125,621	181,858	789,266
Interest expense	162,531	137,823	(15,503)	284,851
Net revenues (expenses)	$ 319,256	$ (12,202)	$ 197,361	$ 504,415
2003				
Unaffiliated revenues	$ 3,059,386	$ 552,718	$ —	$3,612,104
Intersegment revenues	85,425	110,884	(196,309)	—
Total operating revenues	3,144,811	663,602	(196,309)	3,612,104
Unaffiliated expenses	2,435,923	240,460	(315,320)	2,361,063
Depreciation	178,896	171,130	—	350,026
Intersegment expenses	110,401	85,788	(196,189)	—
Total operating expenses	2,725,220	497,378	(511,509)	2,711,089
Net operating revenues	419,591	166,224	315,200	901,015
Interest expense	176,595	168,996	—	345,591
Net revenues (expenses)	$ 242,996	$ (2,772)	$ 315,200	$ 555,424

PRICEWATERHOUSECOOPERS

To the Administrator of the
Bonneville Power Administration,
United States Department of Energy

In our opinion, the accompanying combined balance sheets and the related combined statements of changes in capitalization and long-term liabilities, of revenues and expenses and of cash flows present fairly, in all material respects, the financial position of the Federal Columbia River Power System (FCRPS) at September 30, 2005 and 2004, and the results of its operations and its cash flows for the three years in the period ended September 30, 2005, and the changes in its capitalization and long-term liabilities for each of the two years in the period ended September 30, 2005, in conformity with accounting principles generally accepted in the United States of America. These financial statements are the responsibility of FCRPS' management. Our responsibility is to express an opinion on these financial statements based on our audits. We conducted our audits of these statements in accordance with auditing standards generally accepted in the United States of America. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements, assessing the accounting principles used and significant estimates made by management, and evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

PricewaterhouseCoopers LLP

Portland, Oregon
November 1, 2005

FEDERAL REPAYMENT

Revenue Requirement Study

The revenue requirement study demonstrates repayment of federal investment, and it reflects revenues and costs consistent with BPA's 2002 final power rate proposal in May 2000 for fiscal years 2002 through 2006 (*see* WP-02-FS-BPA-02) and the 2004 final transmission proposal in May 2003 for fiscal years 2004 through 2005 (*see* TR-04-FS-BPA-01). The final proposals filed with FERC, contain the official amortization schedule for the rate periods.

Repayment Demonstration

BPA is required by Public Law 89-448 to demonstrate that reimbursable costs of the FCRPS will be returned to the U.S. Treasury from BPA net revenues within the period prescribed by law. BPA is required to make a similar demonstration for the costs of irrigation projects that are beyond the ability of irrigation water users to repay. These requirements are met by conducting power repayment studies including schedules of payments at the proposed rates to demonstrate repayment of principal within the allowable repayment period.

Since 1985, BPA has prepared separate repayment demonstrations for generation and transmission in accordance with an order issued by the Commission on Jan. 27, 1984 (26 FERC 61,096).

Repayment Policy

BPA's repayment policy is reflected in its generation and transmission revenue requirements and respective rate levels. This policy requires that FCRPS revenues by function be sufficient to:

1. Pay the cost of obtaining power through purchase and exchange agreements (nonfederal projects).
2. Pay the cost of operating and maintaining the power system including payments related to the underfunded status of the CSRS plan.
3. Pay interest on and repay outstanding bonds issued to the U.S.Treasury to finance transmission system construction, conservation, environmental, direct-funded Corps and Reclamation improvements, and fish and wildlife projects.
4. Pay interest on the unrepaid investment in facilities financed with appropriated funds. (Federal hydroelectric projects all were financed with appropriated funds, as were BPA transmission facilities constructed before 1978.)
5. Pay, with interest, any outstanding deferral of interest expense.
6. Repay the power investment in each federal hydroelectric project with interest within 50 years after the project is placed in service (except for the Chandler project, which has a legislated repayment period of 66 years).

7. Repay each increment of the investment in the BPA transmission system financed with appropriated funds with interest within the average service life of the associated transmission plant (40 years).
8. Repay the appropriated investment in each replacement at a federal hydroelectric project within its service life.
9. Repay construction costs at federal reclamation projects that are beyond the ability of the irrigators to pay and are assigned for payment from commercial power net revenues within the same period available to the water users for making payments. These periods range from 40 to 66 years, with 50 years being applicable to most of the irrigation payment assistance.

Investments bearing the highest interest rate will be repaid first, to the extent possible, while still completing repayment of each increment of investment within its prescribed repayment period.

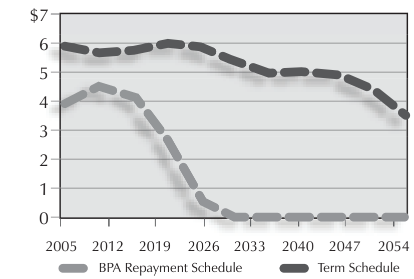
Repayment Obligation

BPA's rates must be designed to collect sufficient revenues to return separately the power and transmission costs of each FCRPS investment and each irrigation assistance obligation within the time prescribed by law.

If existing rates are not likely to meet this requirement, BPA must reduce costs; adjust its rates, or both. However, total

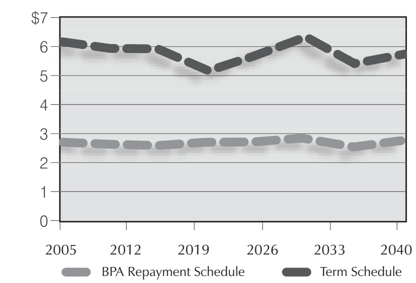
Unrepaid Federal Generation Investment

Includes future replacements — billions of dollars



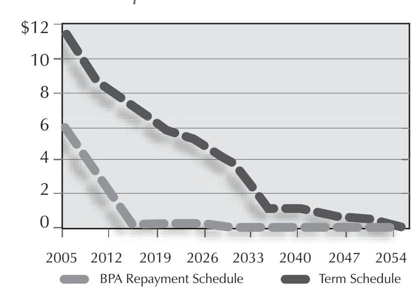
Unrepaid Federal Transmission Investment

Includes future replacements — billions of dollars



Unrepaid Federal Investment

Excludes future replacements — billions of dollars



irrigation assistance payments cannot require an increase in the BPA power rate level. Comparing BPA's repayment schedule for the unrepaid capital appropriations and bonds with a "term schedule" demonstrates that the federal investment will be repaid within the time allowed. A term schedule represents a repayment schedule whereby each capitalized appropriation or bond would be repaid in the year it is due.

Reporting requirements of Public Law 89-448 are met so long as the unrepaid FCRPS investment and irrigation assistance resulting from BPA's repayment schedule are less than or equal to the allowable unrepaid investment in each year. While the comparison is illustrated here by graphs representing total FCRPS generation and total FCRPS transmission investment, the actual comparison is performed on an investment-by-investment basis.

Repayment of FCRPS Investment

The graphs for Unrepaid Federal Generation and Transmission Investment illustrate that unrepaid investment resulting from BPA's generation and transmission repayment schedules is less than the allowable unrepaid investment. This demonstrates that BPA's rates are sufficient to recover all FCRPS investment costs on or before their due dates.

The term schedule lines in the graphs show how much of the obligation can remain unpaid in accordance with the repayment periods for the generation and transmission components of the FCRPS. The BPA repayment schedule lines show how much of the obligation remains to be repaid according to BPA's repayment schedules. In each year, BPA's repayment schedule is ahead of the term schedule. This occurs because BPA plans repayment both to comply with obligation due dates and to minimize costs over the entire repayment study horizon (40 years for transmission, 50 years for generation). Repaying highest interest-bearing investments first, to the extent possible minimizes costs. Consequently, some investments are repaid before their due dates while assuring that all other obligations are repaid by their due dates. These graphs include forecasts of system replacements during the repayment study horizon that are necessary to maintain the existing FCRPS generation and transmission facilities. The Unrepaid Federal Investment graph displays the total planned unrepaid FCRPS obligations compared to allowable total unrepaid FCRPS investment, omitting future system replacements. This demonstrates that each FCRPS investment through 2004 is scheduled to be returned to the U.S. Treasury within its repayment period and ahead of due dates.

If, in any given year, revenues are not sufficient to cover all cash needs including interest, any deficiency becomes an unpaid annual expense. Interest is accrued on the unpaid annual expense until paid. This must be paid from subsequent years' revenues before any repayment of federal appropriations can be made.

BPA 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 40 percent 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 is committed to providing public service and seeks to make its decisions in a manner that provides opportunities for input from all stakeholders.

As part of its public service, 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.

In its vision statement, BPA dedicates itself to providing high system reliability, low rates consistent with sound business principles, environmental stewardship and accountability.

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For the third year in a row, as part of their Earth Day project, dozens of BPA headquarters employees cleaned up 12 miles of paths and helped weed and plant at the 185-acre Hoyt Arboretum in Portland, Ore. Throughout the region, BPA employees participated in local Earth Day activities.

VOLUNTEERING IN THE COMMUNITY

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