Management's Discussion & Analysis

Profile

The Bonneville Power Administration is a federal agency under the Department of Energy. Based in the Pacific Northwest, the agency markets wholesale electrical power from 31 federal hydro projects owned and operated by the U.S. Army Corps of Engineers and Bureau of Reclamation, one nonfederal nuclear plant owned and operated by a consortium of utilities, and several other small nonfederal power plants. BPA also operates and maintains about three-fourths of the region's high-voltage transmission. About one-third of the electric power used in the Northwest comes from BPA.

BPA is a self-funding agency that covers its costs by selling or exchanging wholesale power and related services at cost to meet the needs of consumer-owned utilities and investor-owned utilities in the region. BPA also sells or exchanges power with some large industries in the region and with marketers and utilities in Canada and the western United States. Its service area includes Oregon, Washington, Idaho, western Montana and small parts of Wyoming, Nevada, Utah, California and eastern Montana.

BPA promotes energy efficiency, renewable energy and new technologies. The agency funds regional efforts to protect and enhance fish and wildlife populations affected by hydropower development in the Columbia River Basin. BPA is committed to providing public service and seeks to make its decisions in a manner that provides financial transparency and opportunities for input from all stakeholders.

In its vision statement, BPA dedicates itself to providing high system reliability, low rates consistent with sound business principles, environmental stewardship and accountability. BPA's core values are trustworthy stewardship, collaborative relationships and operational excellence.

General

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

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

Results of Operations

Operating Revenues

For the three months ended Dec. 31, 2009, total operating revenues increased $74 million, or about 10 percent from the comparable period a year earlier, as reported in the Combined Statements of Revenues and Expenses. Power Services gross sales increased $59 million, or 11 percent. The increase is primarily the result of higher rates that went into effect Oct. 1, 2009, partially offset by lower revenues from secondary sales due to reduced runoff and lower market prices. Transmission Services gross sales increased $15 million, or 9 percent, mainly due to ancillary services and point-to-point long-term sales. The ancillary services increase was primarily due to higher rates for wind balancing services that went into effect Oct. 1, 2009, and the installed capacity of wind generation increasing.

The unrealized loss on derivative instruments decreased $31 million for the three months ended Dec. 31, 2009, as compared to the same period in 2008 mainly due to improved mark-to-market valuation on the Libor Interest Rate Swaps as a result of an increase in the 10 and 15 year yield curves.

U.S. Treasury credits for certain fish and wildlife expenditures incurred by BPA increased $2 million, or 10 percent, due to higher capital and program expenses needed for fish mitigation measures in fiscal year 2010 when compared with fiscal year 2009.

Operating Expenses

Operations and maintenance increased $3 million, or 1 percent for the three months ended Dec. 31, 2009, from the comparable period a year earlier due to higher program expenses needed for fish mitigation measures and the Residential Exchange Program in fiscal year 2010 when compared with fiscal year 2009. These increased costs were partially offset by a reduction in the Energy Northwest

Columbia Generating Station nuclear power plant fiscal year 2010 budget as scheduled maintenance and biennial refueling occurred in fiscal year 2009.

Purchased power expense decreased $34 million, or 27 percent, primarily due to lower market prices and volume of purchases resulting from economic conditions for fiscal year 2010 when compared to fiscal year 2009.

Nonfederal projects expense increased $27 million, or 22 percent, primarily due to higher repayment for Energy Northwest's Columbia Generating Station and WNP No.1 terminated nuclear facilities debt. During both periods, restructured nonfederal debt enabled the early repayment of federal debt in lieu of nonfederal debt repayment. Refer to modified net revenues below.

Net Interest Expense

For the three months ended Dec. 31, 2009, allowance for funds used during construction increased $2 million, or 25 percent, with the primary driver being an increase for transmission construction. Interest income decreased $5 million, or 28 percent due to lower cash balances and lower rates earned on U.S. Treasury market-based special securities.

Liquidity and Capital Resources

Net Revenues and Operating Activities

As a result of the factors previously discussed, the FCRPS earned net revenues of $56 million for the three months ended Dec. 31, 2009. By comparison, net expenses were $17 million for the three months ended Dec. 31, 2008.

Cash provided by operating activities of the FCRPS increased $94 million to $44 million for the three months ended Dec. 31, 2009, when compared to the comparable period a year earlier, as reported in the Combined Statements of Cash Flows. The change in operating cash flow primarily reflects the changes in net revenues and differences in the timing of collecting receivables and payments of accounts payable and accrued liabilities. The net change attributable to the Residential Exchange Program was a $83 million inflow.

Investment Activities

When compared to the three months ended Dec. 31, 2008, cash used for investment activities of the FCRPS increased $63 million to $242 million for the three months ended Dec. 31, 2009.

Utility plant investment increased $63 million, driven primarily by investments for additional transmission assets and at generating facilities.

Financing Activities

Compared to $19 million for the comparable period a year earlier, cash provided by financing activities of the FCRPS was $202 million for the three months ended Dec. 31, 2009. BPA borrowed $184 million from the U.S. Treasury during the three months ended Dec. 31, 2009, to fund additional investments. Of the $184 million, $94 million was for transmission investments, $64 million for investments in the Corps and Reclamation projects and $26 million for fish & wildlife investments.

Non-GAAP Financial Information

Modified Net Revenues

Modified net revenues are net revenues after removing the effects of the unrealized loss or (gain) on derivative instruments 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 instruments market prices.

Modified net revenues were $70 million higher for the three months ended Dec. 31, 2009, compared to the comparable period a year earlier, primarily due to the increase in net revenues previously discussed.

The table below demonstrates the calculation for modified net revenues.

Modified Net Revenues

Federal Columbia River Power System
For the fiscal year-to-date ended Dec. 31 — thousands of dollars

	2009	2008
Net revenues (expenses)	**$ 56,225**	$ (16,646)
Derivative instruments	**8,599**	39,947
Nonfederal debt management actions	**(4,744)**	(33,482)
Modified net revenues (expenses)	**$ 60,080**	$ (10,181)

Additional Information

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

To see BPA news, go to www.bpa.gov/corporate/bpanews

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

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

For information about Power Generation, go to www.bpa.gov/power/pg/genspl.shtml

For information on Wind Power, go to www.bpa.gov/corporate/windpower

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

Federal Columbia River Power System
Combined Balance Sheets
(Unaudited)

	Dec. 31, 2009	Sept. 30, 2009
	(thousands of dollars)	
Assets		
Utility plant		
Completed plant	**$ 13,901,769**	$ 13,883,626
Accumulated depreciation	**(5,143,845)**	(5,106,884)
	8,757,924	8,776,742
Construction work in progress	**1,105,369**	985,624
Net utility plant	**9,863,293**	9,762,366
Nonfederal generation	**2,514,885**	2,520,245
Current assets		
Cash	**1,360,740**	1,357,019
U.S. Treasury market-based special securities	**63,921**	14,554
Accounts receivable, net of allowance	**100,624**	112,251
Accrued unbilled revenues	**265,986**	172,842
Materials and supplies, at average cost	**82,540**	77,612
Prepaid expenses	**28,171**	24,652
Total current assets	**1,901,982**	1,758,930
Other assets		
Regulatory assets	**5,088,851**	5,112,346
U.S. Treasury market-based special securities	**131,536**	83,041
Nonfederal nuclear decommissioning trusts	**172,692**	167,232
Deferred charges and other	**225,261**	235,119
Total other assets	**5,618,340**	5,597,738
Total assets	**$ 19,898,500**	$ 19,639,279
Capitalization and Liabilities		
Capitalization and long-term liabilities		
Accumulated net revenues	**$ 2,612,497**	$ 2,556,272
Federal appropriations	**4,414,642**	4,392,405
Borrowings from U.S. Treasury	**1,949,440**	1,765,440
Nonfederal debt	**6,234,289**	6,244,954
Total capitalization and long-term liabilities	**15,210,868**	14,959,071
Commitments and contingencies (See Note 12 to annual financial statements)		
Current liabilities		
Federal appropriations	**3,784**	3,784
Borrowings from U.S. Treasury	**365,000**	365,000
Nonfederal debt	**320,465**	319,980
Accounts payable and other	**506,360**	474,349
Total current liabilities	**1,195,609**	1,163,113
Other Liabilities		
Regulatory liabilities	**2,544,378**	2,567,271
IOU exchange benefits	**83,995**	83,655
Asset retirement obligations	**164,770**	162,943
Deferred credits	**698,880**	703,226
Total other liabilities	**3,492,023**	3,517,095
Total capitalization and liabilities	**$ 19,898,500**	$ 19,639,279

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

	Three Months Ended Dec. 31,		Fiscal Year-to-Date Ended Dec. 31,	
	2009	2008	**2009**	2008
	(thousands of dollars)			
Operating revenues				
Sales	**$ 767,035**	$ 726,519	**$ 767,035**	$ 726,519
Derivative instruments	**(8,599)**	(39,947)	**(8,599)**	(39,947)
U.S. Treasury credits for fish	**23,743**	21,589	**23,743**	21,589
Miscellaneous revenues	**15,294**	14,932	**15,294**	14,932
Total operating revenues	**797,473**	723,093	**797,473**	723,093
Operating expenses				
Operations and maintenance	**352,884**	350,190	**352,884**	350,190
Purchased power	**89,679**	123,390	**89,679**	123,390
Nonfederal projects	**150,852**	123,952	**150,852**	123,952
Depreciation and amortization	**89,859**	88,000	**89,859**	88,000
Total operating expenses	**683,274**	685,532	**683,274**	685,532
Net operating revenues	**114,199**	37,561	**114,199**	37,561
Interest expense and (income)				
Interest expense	**81,771**	81,312	**81,771**	81,312
Allowance for funds used during construction	**(10,141)**	(8,143)	**(10,141)**	(8,143)
Interest income	**(13,656)**	(18,962)	**(13,656)**	(18,962)
Net interest expense	**57,974**	54,207	**57,974**	54,207
Net revenues (expenses)	**$ 56,225**	$ (16,646)	**$ 56,225**	$ (16,646)

Federal Columbia River Power System
Combined Statements of Cash Flows
(Unaudited)

	Fiscal Year-to-Date Ended Dec. 31, 2009	2008
	(thousands of dollars)	
Cash provided by and (used) for operating activities		
Net revenues	**$ 56,225**	$ (16,646)
Non-cash items:		
Depreciation and amortization	**89,859**	88,000
Unrealized loss on derivative instruments	**9,285**	39,976
Changes in:		
Receivables and unbilled revenues	**(79,378)**	(53,975)
Materials and supplies	**(4,928)**	(2,046)
Prepaid expenses	**(3,519)**	1,847
Accounts payable and other	**9,058**	(108,635)
Regulatory assets and liabilities	**(17,939)**	(4,991)
Other assets and liabilities	**(15,112)**	5,729
Cash provided by (used for) operating activities	**43,551**	(50,741)
Cash provided by and (used) for investing activities		
Investment in:		
Utility plant (including AFUDC)	**(146,992)**	(83,568)
Nonfederal generation	**5,360**	5,110
U.S. Treasury market-based special securities:		
Purchases	**(100,000)**	(100,000)
Maturities	**-**	-
Nonfederal nuclear decommissioning trusts	**(2,012)**	(1,962)
Special purpose corporations' trust funds:		
Deposits to	**-**	(23,199)
Receipts from	**1,953**	25,327
Cash used for investing activities	**(241,691)**	(178,292)
Cash provided by and (used) for financing activities		
Federal construction appropriations:		
Increase	**22,236**	16,564
Repayment	**-**	-
Borrowings from U.S. Treasury:		
Increase	**184,000**	-
Repayment	**-**	(35,000)
Nonfederal debt:		
Increase	**-**	23,199
Repayment	**(10,180)**	(9,715)
Customers:		
Advances for construction	**16,608**	27,934
Reimbursements to customers	**(10,803)**	(4,085)
Cash provided by financing activities	**201,861**	18,897
Increase (decrease) in cash	**3,721**	(210,136)
Beginning cash balance	**1,357,019**	1,731,238
Ending cash balance	**$ 1,360,740**	$ 1,521,102
Cash paid for interest, net of U.S. Treasury credits	**$ 5,581**	$ 2,491
Supplemental schedule of noncash operating activities:		
Interest credits	**$ 12,429**	$ 16,982
U. S. Treasury credits	**$ -**	$ -