November 2005

Analyzing Columbia Generating Station debt options for potential rate relief

During the recent Power Function Review process, a customer of the Bonneville Power Administration suggested that BPA analyze the impact of extending a portion of currently outstanding debt for Energy Northwest's Columbia Generating Station as a way to provide some rate relief for the FY 2007-2009 rate period.

The Power Function Review final report stated that BPA would not include the debt extension assumption in the initial power rate proposal but that BPA and Energy Northwest would jointly consider and evaluate its feasibility. BPA committed to review this alternative with customers and other interested parties before including it in the final power rate proposal if such a change is warranted.

The purpose of this fact sheet is to follow up on BPA's commitment in the Power Function Review to share the results of the analysis for review and comment by customers and interested parties. Written comments are welcome anytime between now and Dec. 9, 2005. The comments will be provided to BPA executives and Energy Northwest executive board members for review. For information on how to submit comments, and details on a workshop planned for Nov. 28, 2005, to discuss this topic, please see the last paragraph of this document.

Background

Regional customers and stakeholders understand and appreciate the importance of Energy Northwest's role in supporting BPA's overall debt management objectives while still maintaining its fiduciary responsibilities. On Oct. 27, 2005, BPA staff presented the results of its analysis on extending about $350 million of existing Columbia Generating Station debt to 2024 to the Energy Northwest Audit, Legal and Finance Committee (*www.bpa.gov/corporate/Finance/Debt_Management/presentations/docs/CGS_Debt_EN_Board_10.7.05.pdf*). It is important to be clear that the purpose of the debt extension would be to provide power rate relief for FY 2007-2009. A secondary benefit is that the debt extension would restore some BPA borrowing authority.

BPA and Energy Northwest are also evaluating the feasibility and potential benefit of matching more closely bond maturity dates for new capital investments with the expected lives of those assets. In its analysis, BPA assumed that Columbia Generating Station investments would be financed with maturities through 2024. The initial power rate proposal assumes that these investments will be financed through 2018.

BPA's executives believe the debt extension idea is worth considering for several reasons:

1. This is a timely and economic opportunity to reduce debt service for the FY 2007-2009 period by about $11 million per year with reductions also expected through 2018.

2. This proposed debt management action supports the goal of keeping rates as low as prudently possible since the Northwest economy, although improving, is still fragile.
3. Interest rates for municipal bonds are still at historically low levels, but the interest rate climate is changing and upward pressure on rates is evident.
4. New tax law proposals are currently being considered by Congress that could limit tax-exempt transactions in the future.
5. The current Columbia Generating Station operating license expires in FY 2024, so the extension of Columbia Generating Station debt would better match the expected asset life, a conventional utility practice and BPA's general practice with most other investments.
6. BPA and Energy Northwest will already be in the market for the debt optimization program so this transaction could be combined with that to gain some cost efficiencies.

Financing new Columbia Generating Station investments through 2024 would likely save ratepayers an additional $1.5 million per year in debt service costs for the FY 2007-2009 rate period. This annual benefit increases through 2018 and then becomes more expensive in the 2019-2024 timeframe. Some of the itemized reasons (numbers 2, 3, 5, and 6) above with respect to debt extension also apply to this suggestion.

Overview of results

BPA developed a scenario that extends about $350 million of Columbia Generating Station debt into the 2019-2024 time-frame. This Columbia Generating Station debt is either maturing, callable or advance refundable in 2006, and represents about 16 percent of the approximately $2.2 billion of outstanding Columbia Generating Station debt. Analysis shows that extending this debt reduces BPA's Power Business Line total debt service in FY 2007–2009 by an average of $11 million per year. Further, we expect benefits in future years through 2018, but a slight cost increase in the FY 2019-2024 period. This will be discussed in detail at the workshop on Nov. 28.

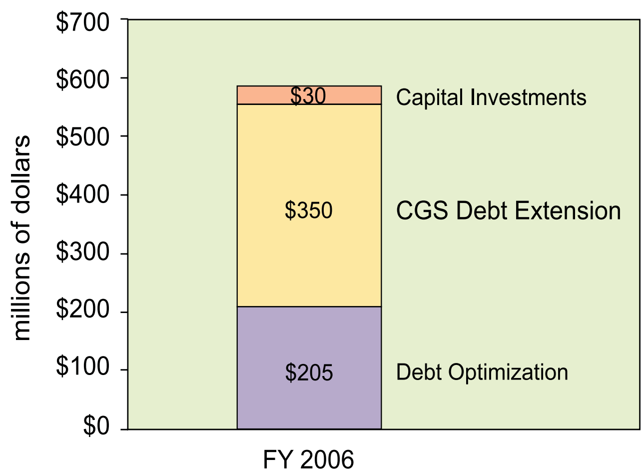
It is important to remember, particularly for approval purposes, that Energy Northwest is the "issuer" of the debt and BPA "backs" their obligation to make debt service payments to bondholders. This arrangement stems from the original net billing agreements entered into by net billing participants, BPA and Energy Northwest.

Although it would be technically possible to extend more than $350 million of debt, BPA is proposing this amount because of tax law considerations. First, we only considered Columbia Generating Station debt ($2.2 billion) for extension, and not the debt for Project 1 ($2.0 billion) or Project 3 ($1.9 billion) because tax counsel for Energy Northwest and BPA have informed us that while extending debt for Projects 1 and 3 might be possible, it is unclear if this would meet all tax law requirements. For this reason, tax counsel did not favor pursuing it. In any case, tax counsel recommended that Columbia Generating Station debt should be extended first before contemplating extending debt on the other two projects.

BPA analyzed extending the bonds to 2024 because the current Columbia Generating Station operating license expires in FY 2024, which coincides with the originally anticipated 40-year expected life of the plant. The IRS allows bonds to be issued with an average life that does not exceed 120 percent of the originally anticipated economic and useful life of the plant (120 percent of 40 years equals 48 years from 1984). Thus, the maturity of the bonds legally could be extended several years past 2024 so long as the average life does not exceed 2032.

Composition of the anticipated spring 2006 financing/refinancing

The extension of $350 million of Columbia Generating Station debt would occur in March/April 2006 at the same time that Energy Northwest and BPA fulfill their commitment to complete a refinancing for the debt optimization program. New bonds would also be issued at this time for $30 million in proposed Columbia Generating Station capital additions. The component pieces of the proposed financing/refinancing are shown below:

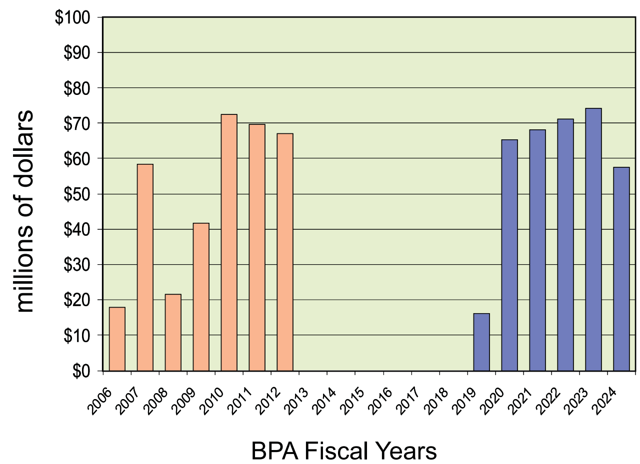


This information was made publicly available by BPA on Oct. 27, 2005. Actuals may vary from this forecast.

Proposed changes in principal maturity dates

BPA manages all parts of its outstanding liabilities (federal appropriations, federal bonds, third-party debt, lease transactions) using a holistic approach. The chart below isolates the $350 million Columbia Generating Station debt extension we modeled to assist the reader in understanding the idea. It shows how the current $350 million in principal for the existing Columbia Generating Station debt would be moved from the 2006-2012 period to 2019-2024 as a result of the debt extension. The bars on the left side of the chart indicate the years in which the $350 million in principal is currently scheduled to be paid and the bars on the right indicate the years it would be paid under the exten-sion assumption. Of course, ratepayers would continue to pay interest on the debt at the rate at which the bonds are issued in the spring of 2006, but the bonds would not mature and be paid off until the 2019-2024 period.

Debt optimization and this potential Columbia Generating Station debt extension both involve the extension of debt but they are distinct and separate programs, each designed with a different goal in mind. Both financings would be completed at the same time. We plan to address the impacts of extending Columbia Generating Station debt on the current debt optimization program at the workshop.



This information was made publicly available by BPA on Oct. 27, 2005. Actuals may vary from this forecast.

What happens next?

BPA is planning a workshop for customers and other stakeholders to discuss this proposal in more detail and to answer any questions. The workshop is scheduled for Nov. 28, 2005, from 3 to 5 p.m. in the BPA Rates Hearing Room, at 905 N.E. 11th Ave., Portland, OR 97232. Written comments on this proposal may be submitted online at *www.bpa.gov/corporate/public_affairs/comment.cfm* or they can be e-mailed to: *comment@bpa.gov*. You may submit comments in hard copy by mailing to: Bonneville Power Administration DKP-7, P.O. Box 14428, Portland, OR 97293-4428. If you cannot attend in person and wish to join the meeting by phone, please call Joyce Chan, at (503) 230-5863.

BPA will accept public comments on the subject until Dec. 9, 2005. It will then summarize the comments, post the summary, and provide it to the Energy Northwest Audit, Legal and Finance Committee for its consideration. Final approval from the Energy Northwest Executive Board, if warranted, must occur on Jan. 26, 2006, when the Energy Northwest Executive Board approves the Energy Northwest FY 2006 Plan of Finance, before bonds can be sold in the capital markets. The bonds would be priced sometime around the middle of March in conjunction with the annual debt optimization bond issuance, and the transaction would close in April. Then BPA will work to finalize the repayment studies to include the resulting rate reduction in the Power Business Line final rate proposal. This schedule is summarized in the timeline graphic below.

If you have any questions about this topic, please bring them to the Nov. 28 workshop or contact Anita Mertsching at (503) 230-3413 or Don Carbonari at (503) 230-3798. However, please remember that ex parte began Nov. 8. While debt management practices are not part of the rate case, BPA prefers to only discuss the possible rate impacts of Columbia Generating Station debt extension at noticed meetings.