

2011 Annual Report

Management's Discussion & Analysis

Securing the Future



Management’s Discussion & Analysis

Table of Contents

Forward-Looking Information.....	1
Management’s Discussion & Analysis.....	4
Federal Repayment	16

Refer to Audited Financial Statements for Financial Statements and Notes to Financial Statements.



Forward-Looking Information

This forward-looking information contains statements which, to the extent they are not recitations of historical fact, constitute “forward-looking statements.” In this respect, the words “estimate,” “project,” “anticipate,” “expect,” “intend,” “believe” and similar expressions are intended to identify forward-looking statements. A number of important factors affecting Bonneville Power Administration’s business and financial results could cause actual results to differ materially from those stated in the forward-looking statements. BPA does not plan to issue any updates or revisions to the forward-looking statements.

INFRASTRUCTURE

Infrastructure of the Federal Columbia River Power System is aging, both hydro projects and the transmission system. Not only does this increase cost pressures on operations and maintenance, but it also means the system may be vulnerable in terms of reliability. Making planned investments will reduce the likelihood of forced outages. This issue is central to protecting the value and assets of the FCRPS. Building or replacing infrastructure does not directly impact current rates, but the resulting interest and depreciation will impact rates many years into the future. In addition, BPA must maintain adequate cash reserves to cover the cash requirements to repay Treasury.

Infrastructure investments also can be affected by economic, policy and commercial considerations. For example, BPA had planned to award a construction contract for its Central Ferry-Lower Monumental 500-kilovolt transmission project in fiscal year 2011, but deferred that action when wind generator parties that had signed Preliminary Transmission Service Agreements to use the transmission indicated that their loads were not growing as quickly as they had expected. Transmission projects are particularly subject to public concerns and the relative immediacy of need for each project.

AVAILABILITY OF CAPITAL

BPA’s capital program calls for investment of \$6.4 billion in energy efficiency, power generation, transmission and fish and wildlife assets in fiscal years 2011-2017. Without adjustments to capital sources, this could exhaust BPA’s existing Treasury borrowing authority by fiscal year 2016. BPA anticipates using third-party financing and potentially other tools for appropriate capital investments and is conferring with its customers and interested parties on its capital investment priorities and financing alternatives. Failure to plan and prioritize effectively could affect timing of needed investments and possibly system reliability and availability.

COLUMBIA GENERATING STATION

Energy Northwest, a joint operating agency of the State of Washington formed and maintained by certain municipal utilities and utility districts, owns and operates Columbia Generating Station, the region’s only operating commercial nuclear plant. BPA funds the plant and markets its energy. The plant represents a significant portion of BPA’s wholesale power rates, with annual operations and maintenance costs on average roughly equaling the similar costs for the 31 federal dams that produce close to 90 percent of BPA’s power.

For several years, Columbia Generating Station has had to address a number of performance challenges such as unplanned outages, unscheduled power reductions and long refueling outages. BPA and Energy Northwest are working together to address plant performance and have agreed on steps to move forward. Energy Northwest is focusing on improved plant reliability. This year, Energy Northwest replaced the main condenser of the plant. The condenser replacement took longer and cost more than planned, but BPA believes this major investment should help improve future plant performance. The plant is a valuable carbon-free resource that is being operated safely. In the future, if carbon costs are included in electricity pricing, BPA would expect the plant to become even more valuable.

TIERED RATES

At the end of calendar year 2008, BPA signed new wholesale power sales contracts with its preference customers and certain other agreements with some investor-owned utilities for fiscal years 2012-2028. In addition, BPA issued the Tiered Rate Methodology at about the same time, which was the result of several years of negotiations among BPA and its customers. The new contracts together with the Tiered Rate Methodology provide BPA and its preference customers with greater long-term rate stability.

Tiered rates went into effect on Oct. 1, 2011, for fiscal year 2012. Preference customers have a contractually defined right to purchase an amount of power at Tier 1 rates. The aggregate amount of power available at Tier 1 rates is limited to the output of the existing resources of the federal system, subject to certain possible limited adjustments. Tier 1 rates are expected to remain relatively low and stable because they recover the cost of the existing federal system, which in aggregate is expected to continue as a low cost portfolio of generating resources.

ENDANGERED SPECIES ACT

In 1991 and subsequent years, the federal government listed certain fish species that are affected by operation of the federal system's Columbia River and Snake River dams as endangered or threatened. Since that time, the federal government has prepared several "biological opinions" that sought to address, among other things, the means by which the federal system dams may be operated without jeopardizing the existence of the listed species. These prior biological opinions were challenged successfully in court. In 2008, the federal government issued a 2008 Federal Columbia River Power System Biological Opinion. The government supplemented the 2008 biological opinion in 2010 with additional information. The 2008 biological opinion and the 2010 supplemental information were then challenged in court. On Aug. 2, 2011, the court remanded these biological opinions to National Oceanic and Atmospheric Administration Fisheries, citing insufficient specificity on post-2013 habitat improvements. The court ordered submission of a new or revised biological opinion by Jan. 1, 2014, listing specific habitat improvements for 2014-2018. The 2010 BiOp with court-ordered spill remains in effect through 2013.

Because the biological opinion governs how the federal hydropower system should be operated to protect salmon and steelhead listed under the Endangered Species Act and establishes fish and wildlife programs that aid in avoiding jeopardy of the species, the ultimate outcome of this litigation could have major financial consequences by affecting the electric generation of the system and the costs that BPA faces.

VARIABLE ENERGY RESOURCE INTEGRATION

The rapidly increasing penetration of wind power in BPA's transmission grid already has necessitated significant changes in BPA's transmission operating protocols and practices and is driving changes in transmission operations west-wide. West-wide discussions of an energy imbalance market, interregional transmission expansion, widespread intra-hour power marketing and emerging use of smart grid technologies, if successful, could bring new efficiencies, economies and environmental benefits to consumers. However, there is also the possibility that overbuilt wind generation could become trapped in the Pacific Northwest, creating price distortions in energy markets.

Management's Discussion & Analysis

Results of operations

OPERATING REVENUES

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

	2011	2010	2009
Gross sales:			
Power	\$ 2,486,801	\$ 2,233,570	\$ 2,090,387
Transmission	739,606	738,330	689,197
Bookouts	(92,198)	(120,803)	(36,814)
Sales	3,134,209	2,851,097	2,742,770
Derivative instruments	—	14,800	(34,677)
U.S. Treasury credits for fish	85,102	123,090	99,499
Miscellaneous revenues:			
Power	29,299	33,969	37,982
Transmission	36,164	32,175	24,710
Total operating revenues	\$ 3,284,774	\$ 3,055,131	\$ 2,870,284

Fiscal year 2011 revenues compared to fiscal year 2010

For the fiscal year ended Sept. 30, 2011, Power Services and Transmission Services consolidated gross sales increased \$255 million, or 9 percent, from the prior year.

Power Services gross sales increased \$253 million, or 11 percent. The change was primarily due to the following key factors:

- Firm sales increased \$72 million, or 4 percent, in fiscal year 2011 compared to fiscal year 2010 due to higher priority firm sales resulting from higher firm loads and inclusion of slightly higher stepped rates for a few customers. In addition, 2011 had higher revenues from sales to direct-service industries as DSI contracts were not fully in place at the beginning of fiscal year 2010.
- Secondary sales increased \$180 million, or 59 percent, in fiscal year 2011 compared to fiscal year 2010 due to much higher streamflows. A typical metric to measure runoff is million acre feet. January through July runoff volume at the Dalles Dam was 142 maf, the fourth highest on record for the runoff season. The full fiscal year 2011 October through September volume finished as the sixth highest water year on record at 175 maf, a significant increase from 110 maf in fiscal year 2010 and above the historical average of 133 maf.

- Power gross sales increased to 93,557,046 megawatt-hours in fiscal year 2011 from 76,545,126 megawatt-hours in fiscal year 2010, or 22 percent. The effect of higher streamflows on revenues from secondary sales was partially offset by slightly lower average prices in fiscal year 2011 compared to fiscal year 2010. In addition, unplanned extensions of planned maintenance outages at Columbia Generating Station and at a turbine in the Grand Coulee Third Powerhouse reduced agency power sales revenues by an estimated \$65 million from what would have been expected had the extended outages not occurred.

Bookouts are presented on a net basis in the Combined Statement of Revenues and Expenses. When sales and purchases are scheduled with the same counterparty on the same path for the same hour, the power is typically booked out and not scheduled for physical delivery. The megawatt-hours that offset each other net to zero. The dollar values of these offsetting transactions are recorded as bookouts. The result is that revenues and expenses are presented on a net basis in the Combined Statements of Revenues and Expenses. Therefore the accounting treatment for bookouts has no effect on net revenues, cash flows or margins.

Derivative instruments decreased to zero in fiscal year 2011 compared to \$15 million unrealized gain at the end of fiscal year 2010. The change resulted from the application of Regulated Operations accounting treatment beginning in fiscal year 2010 to the unrealized gains and losses related to certain power purchase and power sale contracts. As a result these amounts are recorded on the Combined Balance Sheets under Regulatory assets or Regulatory liabilities rather than in the Combined Statements of Revenues and Expenses.

U.S. Treasury credits for fish decreased to \$85 million in fiscal year 2011 from \$123 million in fiscal year 2010, or about 31 percent. The change was primarily due to increased streamflows and higher federal generation which decreased the need for purchased power. This resulted in lower purchased power costs which were partially offset by higher direct program costs for fish mitigation.

Fiscal year 2010 revenues compared to fiscal year 2009

For the fiscal year ended Sept. 30, 2010, Power Services and Transmission Services consolidated gross sales increased by \$192 million, or 7 percent, from the prior year.

Power Services gross sales increased \$143 million, or 7 percent. The change was primarily due to the following key factors:

- Firm sales increased \$164 million in fiscal year 2010 compared to fiscal year 2009 due to higher rates in fiscal year 2010. The Wholesale Power 2010 Rate Case established BPA power rates for fiscal years 2010 and 2011. As a result, the Priority Firm preference average rates were \$28.77 per megawatt-hour in fiscal year 2010 compared with \$26.90 per megawatt-hour in fiscal year 2009. The Slice PF rate was 4.8 percent higher in fiscal year 2010 than in fiscal year 2009. The rate increase for fiscal year 2010 was 7 percent on average for non-Slice customers.
- Secondary sales decreased \$22 million in fiscal year 2010 compared to fiscal year 2009 due to lower than average streamflows and hydro generation. Basin-wide precipitation and streamflows were well below normal during the first half of fiscal year 2010. Although the June record rainfall increased streamflows, it was not enough to overcome the precipitation deficit that occurred early in the year.

Runoff measured at The Dalles Dam was 110 maf and 117 maf for fiscal years 2010 and 2009, respectively, compared to the historical average of 131 maf.

- Power gross sales increased slightly to 76,545,126 MWh in fiscal year 2010 from 76,421,688 MWh in fiscal year 2009. Columbia Generating Station output increased 33 percent to 9,003,577 MWh in fiscal year 2010 compared to 6,775,649 MWh in fiscal year 2009. Reduced CGS output in fiscal year 2009 was due to planned outages for maintenance and refueling, and unplanned outages.

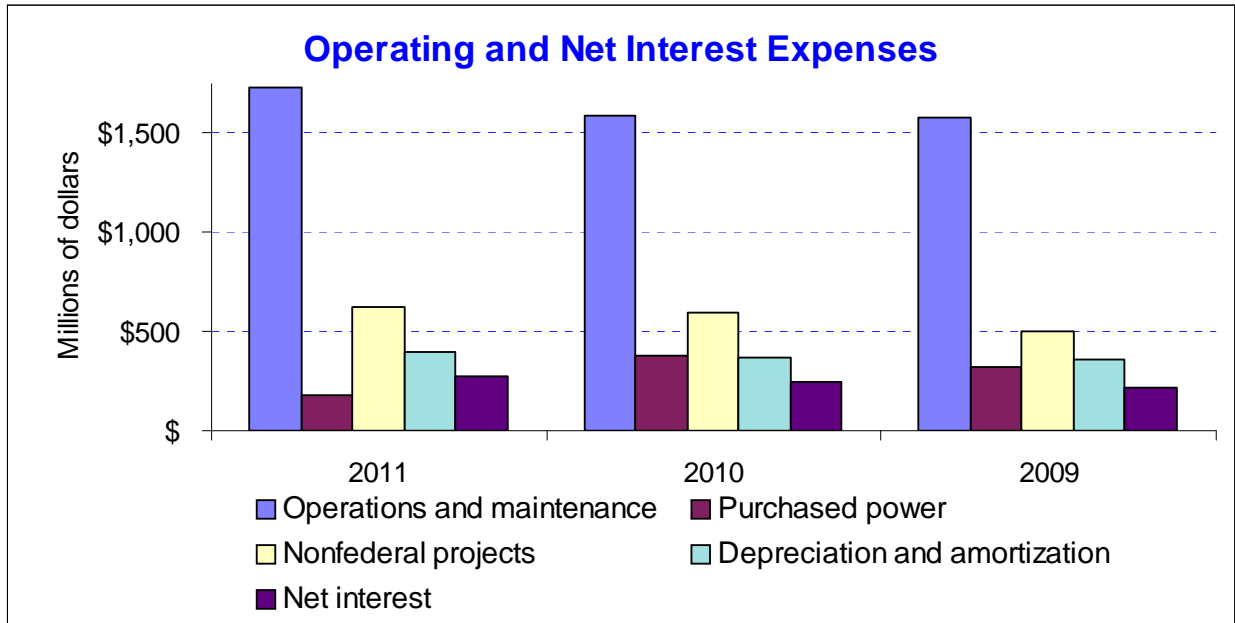
Transmission Services gross sales increased \$49 million, or 7 percent, in fiscal year 2010 from the prior year, mainly due to Network and Ancillary Service product sales.

- Point-To-Point long-term and Network Integration revenues increased by \$15 million and \$4 million, respectively, due to overall increases in transmission reservations and product deliveries.
- Ancillary Services products increased by \$30 million. Higher rates for Within-Hour Balancing Resources and for Operating Reserves caused \$27 million of the increase, and Energy and Generation Imbalance sales, driven in part by additional wind generation, increased \$3 million.

The change in derivative instruments to an unrealized gain of \$15 million in fiscal year 2010 from an unrealized loss of \$35 million in fiscal year 2009 was primarily due to the following factors:

- BPA's termination of its LIBOR interest rate swaps in February 2010.
- BPA's application of regulatory operations accounting to its derivative instruments. Regulatory operations accounting was applied in conjunction with the finalization of BPA's new long-term Tier 2 power sales contracts in 2010, and means that unrealized gains and losses from derivative instruments are recorded as Regulatory assets and liabilities on the Combined Balance Sheet as opposed to Operating revenues on the Combined Statement of Revenues and Expenses.
- The unrealized gain of \$15 million recorded in Operating revenues in fiscal year 2010 represents the reversal of the ending unrealized loss position for fiscal year 2009, which was the net of a gain position on commodity contracts and a loss position on the LIBOR interest rate swaps.

U.S. Treasury credits for fish increased to \$123 million in fiscal year 2010 from \$99 million in fiscal year 2009, or about 24 percent. The change was primarily due to below normal streamflows, increased purchased power and increases in program expenses.



Fiscal year 2011 expenses compared to fiscal year 2010

For the fiscal year ended Sept. 30, 2011, operating expenses decreased \$9 million from fiscal year 2010.

Operations and maintenance increased \$145 million, or 9 percent, from the prior fiscal year, as reported in the Combined Statements of Revenues and Expenses, due mainly to increases of \$65 million for maintenance and biennial refueling for the Columbia Generating Station. Other year-over-year increases were Transmission Services operations and maintenance of \$23 million, Fish and Wildlife Program of \$22 million, and other agency expenses of \$14 million. Fish and wildlife increases were driven by changes in the Northwest Power and Conservation Council's Columbia River Basin Fish and Wildlife Program and in the Endangered Species Act biological opinions. In addition certain defective transmission line spacer dampers were impaired, resulting in a \$21 million impairment charge.

Purchased power expenses decreased \$204 million, or 53 percent, mainly due to higher streamflows during the current fiscal year when compared to the prior fiscal year. Higher streamflows contributed to increased federal generation, which reduced the amount of power purchased to meet load.

Nonfederal projects debt service increased \$25 million, or 4 percent, due to higher bond principal payments of \$204 million for Energy Northwest's Projects Nos. 1 and 3. The increase was offset by a reduction of \$143 million for Columbia Generating Station. Another reduction was the non-recurrence in fiscal year 2011 of a one-time-only \$34 million termination fee for two floating-to-fixed LIBOR interest rate swaps which occurred in fiscal year 2010. Over the past two decades, Energy Northwest's debt service has been periodically restructured to achieve overall federal and nonfederal debt service objectives that reduced nonfederal projects expense. These debt management actions have created an uneven Energy Northwest debt service structure such that there can be significant variances from year to year.

Depreciation and amortization increased \$25 million, or 7 percent from the prior fiscal year, primarily due to increases for conservation amortization of \$10 million and depreciation on transmission assets of \$8 million, consistent with increases in capital expenditures.

Net interest expense for the fiscal year ended Sept. 30, 2011, increased \$29 million, or 12 percent, compared to fiscal year 2010. The primary drivers were \$15 million of call premiums paid for refinancing bonds issued to the U.S. Treasury and a \$17 million, or 32 percent, reduction of interest income as a result of lower cash balances and interest rates. Consistent with an agreement with the U.S. Treasury, annually increasing amounts of BPA's reserve balance have been and will be invested in U.S. Treasury market-based special securities in lieu of accruing interest rate credits based on the weighted average interest rate of BPA's outstanding bonds issued to the U.S. Treasury.

Fiscal year 2010 expenses compared to fiscal year 2009

For the fiscal year ended Sept. 30, 2010, operating expenses increased \$186 million, or 7 percent, from fiscal year 2009.

Operations and maintenance increased \$11 million from the prior fiscal year as reported in the Combined Statements of Revenues and Expenses. Increased expenses were primarily for the Fish and Wildlife Program of \$24 million driven by the Northwest Power and Conservation Council's Columbia River Basin Fish and Wildlife Program and biological opinions, direct funded federal hydro projects of \$18 million for system operations and maintenance, Energy Efficiency Program of \$6 million driven primarily by federal energy efficiency reimbursable projects, Transmission Operations Program of \$5 million due to substation operations, scheduling and technical operations and miscellaneous expenses of \$14 million. These increases were partially offset by decreased expenses of \$31 million for Columbia Generating Station associated with scheduled refueling and maintenance and Residential Exchange Program payments of \$25 million primarily due to the Avista settlement that occurred in 2009.

Gross purchased power increased \$104 million, or 37 percent, mainly due to below normal basin-wide precipitation and stream flows not providing sufficient generation to fulfill load obligations. The increase was partially offset by a \$40 million reduction due to discontinuing payments in lieu of power deliveries to the direct-service industries, consistent with a Ninth Circuit Court opinion. Operations to allow for fish mitigation measures also contributed to the need to purchase additional power.

Nonfederal projects debt service increased \$99 million, or 20 percent, primarily due to an increase in bond principal payments of \$96 million for Energy Northwest's Project 1 and Columbia Generating Station.

Net interest expense for the fiscal year ended Sept. 30, 2010, increased \$25 million, or 11 percent, compared to fiscal year 2009 primarily due to a \$22 million decrease in interest income as a result of lower cash balances and interest rates.

Selected quarterly information

Due to autumn and winter heating loads for Northwest utilities, first and second quarters normally have the highest revenues. Maintenance on transmission facilities increases during summer, usually resulting in higher operating expenses for fourth quarters.

Selected quarterly information

Federal Columbia River Power System
3 months ended (thousands of dollars)

	Dec 31	Mar 31	Jun 30	Sep 30	Totals
2011					
Operating revenues	\$ 851,022	\$ 931,689	\$ 730,822	\$ 771,241	\$ 3,284,774
Operating expenses	736,585	707,562	708,876	777,710	2,930,733
Net interest expenses	64,813	62,941	63,274	81,331	272,359
Net revenues (expenses)	\$ 49,624	\$ 161,186	\$ (41,328)	\$ (87,800)	\$ \$81,682
2010					
Revenues	\$ 806,072	\$ 804,588	\$ 725,046	\$ 704,625	\$ 3,040,331
Derivative instruments	(8,599)	16,585	6,814	—	14,800
Operating revenues	797,473	821,173	731,860	704,625	3,055,131
Operating expenses	683,274	784,180	670,008	801,908	2,939,370
Net interest expenses	57,974	59,467	59,475	66,426	243,342
Net revenues (expenses)	\$ 56,225	\$ (22,474)	\$ 2,377	\$(163,709)	\$ (127,581)
2009					
Revenues	\$ 763,040	\$ 787,348	\$ 700,961	\$ 653,612	\$ 2,904,961
Derivative instruments	(39,947)	4,924	2,957	(2,611)	(34,677)
Operating revenues	723,093	792,272	703,918	651,001	2,870,284
Operating expenses	685,532	688,465	624,871	754,037	2,752,905
Net interest expenses	54,207	53,093	60,763	50,366	218,429
Net (expenses) revenues	\$ (16,646)	\$ 50,714	\$ 18,284	\$(153,402)	\$ (101,050)

Liquidity and capital resources

OPERATING ACTIVITIES

As a result of the factors previously discussed, the Federal Columbia River Power System earned net revenues of \$82 million for the fiscal year ended Sept. 30, 2011. By comparison, the FCRPS incurred net expenses of \$128 million for the fiscal year ended Sept. 30, 2010. Net cash provided by operating activities of the FCRPS increased to \$437 million for the fiscal year ended Sept. 30, 2011, as reported in the Combined Statements of Cash Flows.

Net cash provided by operating activities of the FCRPS increased to \$370 million for the fiscal year ended Sept. 30, 2010, from \$268 million for fiscal year ended Sept. 30, 2009, as reported in the Combined Statements of Cash Flows. By further comparison, net expenses were \$101 million for the fiscal year ended Sept. 30, 2009. The changes in operating cash flow primarily reflects differences in the timing of collecting receivables, payments of accounts payable and accrued liabilities. Cash used for operating activities also includes expenditures for regulatory assets, such as the conservation and fish and wildlife programs.

INVESTING ACTIVITIES

Net cash used for investing activities of the FCRPS increased \$271 million to \$983 million for the fiscal year ended Sept. 30, 2011, when compared to the fiscal year ended Sept. 30, 2010. Investment in utility plant increased \$104 million, driven primarily by investments for additional transmission assets and at generating facilities.

BPA invested \$100 million in U.S. Treasury market-based special securities at the beginning of both fiscal years. Under its banking arrangement with the U.S. Treasury, BPA agreed to increase the amount invested in market based specials by \$100 million per year through fiscal year 2018 or until the BPA fund is fully invested. During the fiscal year ended Sept. 30, 2011, \$163 million of investments and \$45 million of cash equivalents matured and were re-invested in other market-based special securities. BPA's current investment portfolio consists of primarily short-term securities.

In the fiscal year ended Sept. 30, 2011, the consolidated special purpose corporations deposited \$106 million into their restricted trust funds and transferred \$67 million to the BPA fund to support construction activities on leased transmission projects. When compared to the same activities for the fiscal year ended Sept. 30, 2010, the \$75 million net change reflects an increase in construction activity on leased projects as seen by increases in both deposits to the restricted trust funds and advances to the BPA fund.

Net cash used for investing activities of the FCRPS decreased \$63 million to \$713 million for the fiscal year ended Sept. 30, 2010, when compared to the fiscal year ended Sept. 30, 2009. Utility plant investment increased \$109 million, driven primarily by investments for additional transmission assets and at generating facilities. During the fiscal year, \$45 million of investments matured and were re-invested into 90-day securities. In the fiscal year ended Sept. 30, 2010, the consolidated special purpose corporations deposited \$5 million into their restricted trust funds and transferred \$40 million to the BPA fund to support transmission construction activities on leased projects. When compared to the same activities for the fiscal year ended Sept. 30, 2009, the \$127 million net change reflects a reduction in construction activity on leased projects as seen by decreases in both deposits to the restricted trust funds and transfers to the BPA fund.

FINANCING ACTIVITIES

Net cash provided by financing activities of the FCRPS was \$360 million for the fiscal year ended Sept. 30, 2011, compared to \$64 million for the fiscal year ended Sept. 30, 2010. Bond principal payments may differ from those scheduled in prior years as a result of current year management actions. For example, in fiscal year 2011 BPA refinanced \$354 million of U.S. Treasury bonds at a lower rate of interest and paid a \$15 million call premium to do so. Federal appropriations increased compared to the prior fiscal year primarily due to \$165 million lower repayment and \$43 million higher funding for capital investments and operations and maintenance at federal generating facilities. BPA borrowings from the U.S. Treasury were \$800 million, an increase of \$162 million, while U.S. Treasury bond repayment was \$370 million, an increase of \$115 million. The \$800 million in bonds issued to the U.S. Treasury in fiscal year 2011 include \$370 million for transmission investments, \$235 million for generation investments, \$80 million for fish and wildlife investments and \$115 million for conservation investments. Additional nonfederal debt of \$202 million was issued under the Lease Financing Program, \$96 million of which were issued in order to refinance \$90 million at a beneficially lower interest rate. Increased nonfederal debt repayments were primarily due to an increase of \$91 million and \$85 million for Energy Northwest's Projects Nos. 1 and 3, respectively, partially offset by a reduction in debt repayments of \$141 million for Columbia Generating Station.

Cash provided by financing activities of the FCRPS was \$64 million for the fiscal year ended Sept. 30, 2010, compared to \$133 million for the fiscal year ended Sept. 30, 2009. Federal appropriations decreased primarily due to \$166 million higher repayment and \$90 million lower funding for capital investments and operations and maintenance at federal generating facilities. BPA borrowings from the U.S. Treasury increased \$300 million during the fiscal year to \$638 million while repayment decreased \$138 million to \$255 million. Of the \$638 million in new borrowings from the U.S. Treasury, \$349 million were for transmission investments, \$243 million for generation investments and \$46 million for fish and wildlife investments. American Recovery and Reinvestment Act funds are being used to fund in part investments across these classes. Nonfederal debt issued in fiscal year 2010 decreased \$195 million compared to fiscal year 2009 as a result of reduced Lease Financing Program borrowings for transmission infrastructure. Increased nonfederal debt repayments were primarily due to an increase of \$96 million for Energy Northwest's Project 1 and Columbia Generating Station.

CASH AND CASH EQUIVALENTS BALANCE AND BPA RESERVES

At Sept. 30, 2011, the FCRPS ending cash and cash equivalents balance on the Combined Balance Sheet was \$892 million. BPA's fiscal year-end cash and cash equivalents balance, excluding funds transferred from the Spectrum Relocation fund, was \$601 million, and the Corps and Reclamation combined fiscal year-end cash balance was \$291 million.

BPA's year-end reserves for fiscal years 2011, 2010 and 2009 were \$1.01 billion, \$1.11 billion and \$1.36 billion, respectively. For fiscal year 2011, financial reserves are comprised of BPA cash, investments in U.S. Treasury market-based special securities and deferred borrowing. The U.S. Treasury market-based special securities reflect the market value as if securities were liquidated at Sept. 30, 2011. Deferred borrowing represents amounts that BPA is authorized to borrow from the U.S. Treasury for expenditures that BPA has incurred but has not borrowed for as of Sept. 30, 2011.

BPA BORROWING AUTHORITY FROM THE U.S. TREASURY

The aggregate principal amount of debt BPA is authorized to have outstanding with the U.S. Treasury at any one time is \$7.70 billion. This amount includes \$3.25 billion in borrowing authority from the U.S. Treasury provided in the American Recovery and Reinvestment Act. The U.S. Treasury borrowing authority may be used to finance BPA's capital programs, and in certain cases for operating expenses relating to implementation of the Northwest Power Act. BPA and the U.S. Treasury have agreed to a short-term line of credit enabling BPA to borrow up to \$750 million for Pacific Northwest Electric Power Planning and Conservation Act expenses. For capital programs, the related U.S. Treasury debt is term limited depending on the facilities financed: 50 years for Corps and Reclamation capital investments, 35 years for transmission facilities, 15 years for fish and wildlife and environment projects and 12 years for conservation projects. As of Sept. 30, 2011, BPA had \$2.94 billion of bonds outstanding with the U.S. Treasury. The original terms of the outstanding U.S. Treasury borrowings vary from four to 30 years. All debt issued to the U.S. Treasury after Apr. 30, 2008, is issued with call options exercisable by BPA. At Sept. 30, 2011, BPA had 89 callable borrowings on its books totaling \$2.47 billion. The interest on BPA's outstanding borrowings from U.S. Treasury is set at fixed and variable rates comparable to the rates prevailing in the market for similar bonds issued by government corporations. As of Sept. 30, 2011, the interest rates on the outstanding U.S. Treasury borrowings ranged from 1.4 percent to 6.4 percent with a weighted-average interest rate of approximately 4.2 percent. At Sept. 30, 2011, there were no outstanding bonds with a variable rate of interest.

LEASE FINANCING PROGRAM

The Lease Financing Program enables BPA to continue to invest in infrastructure to support a safe and reliable system for the transmission of power with an alternative to the use of limited statutory borrowing authority with the U.S. Treasury. Under this program, BPA has entered into lease arrangements with five special purpose corporations. These entities are collectively referred to as the Northwest Infrastructure Financing Corporations and are consolidated by BPA for financial statement reporting purposes.

From inception through fiscal year 2011, BPA has entered into lease arrangements for \$556 million with the NIFCs for specific transmission assets. BPA is the construction agent to construct and install the leased assets. The construction costs of the assets are being financed through bonds issued by the NIFCs or by bank lines of credit entered into by the NIFCs. The related debt service is paid from and secured solely by BPA's lease payments and amounts held in trust funds established by the NIFCs. The related transmission assets are not pledged as security for repayment of the related loans or bonds. The lease agreements expire between fiscal years 2014 and 2016 and in 2034, at which point BPA may acquire the assets, negotiate the extension of the leases for longer terms, or arrange for the transfer of the assets to a separate owner and lease the assets from the new owner.

TREASURY PAYMENT

BPA paid the U.S. Treasury \$830 million for fiscal year 2011, making it the 28th consecutive year in which BPA has made its payments on time and in full. The fiscal year 2011 payments included \$410 million in principal and \$382 million in interest for U.S. Treasury debt and for the appropriated federal investment in the FCRPS. This fiscal year's principal payment included \$70 million to repay bonds issued to the U.S. Treasury in excess of the base payment calculated for the Federal Energy Regulatory Commission filings. BPA paid the U.S. Treasury \$38 million in other obligations, including \$31 million of additional funding for post-retirement benefit programs provided to employees associated with the operation of the FCRPS. Payments made in fiscal years 2010 and 2009 were \$864 million and \$845 million, including \$39 million

and \$234 million, respectively, to repay federal appropriations and bonds issued to the U.S. Treasury in excess of the base payments calculated for FERC filings. As previously discussed, over the past two decades, Energy Northwest's debt service was periodically restructured to achieve overall federal and nonfederal debt service objectives which reduced nonfederal projects expense and accelerated principal payments of federal appropriations and bonds issued to the U.S. Treasury.

CREDIT RATINGS

Credit ratings on nonfederal debt backed by BPA at Sept. 30, 2011, were as follows:

- Moody's at Aa1 with a stable outlook
- Standard & Poor's at AA- with a stable outlook
- Fitch at AA with a stable outlook

Contractual obligations and federal payments

Amounts shown in the following table for federal appropriations, borrowings from U.S. Treasury and nonfederal debt include interest expense and are therefore higher than amounts for these line items reflected in the Combined Balance Sheets and described in the Notes to Financial Statements - Note 6, Federal Appropriations; Note 7, Borrowings from U.S. Treasury; and Note 8, Nonfederal Financing. Asset retirement obligations also include interest and are described in Note 4, Asset Retirement Obligations. Capital leases include interest and are described in Note 10, Deferred Credits and Other. Purchase power commitments are a period expense. Irrigation assistance is treated as a distribution from accumulated net revenues when paid. Purchase power commitments and Irrigation assistance are described in Note 13, Commitments and Contingencies.

Contractual obligations and federal payments

As of Sept. 30 (thousands of dollars)

	2012	2013	2014	2015	2016	2017+	Total
Federal appropriations	\$ 271,486	\$ 263,351	\$ 262,985	\$ 297,187	\$ 238,416	\$ 10,027,844	\$ 11,361,269
Borrowings - U.S. Treasury	387,927	235,822	209,095	182,948	131,498	3,624,669	4,771,959
Nonfederal debt	739,281	783,711	980,434	1,020,638	1,036,043	3,661,052	8,221,159
Asset retirement obligations	12,397	13,312	14,740	18,220	26,543	590,979	676,191
Capital leases	4,948	4,759	4,759	4,759	4,759	90,325	114,309
Purchase power commitments	51,805	66,441	35,234	—	—	—	153,480
Irrigation assistance	1,182	58,823	52,427	51,989	60,814	440,855	666,090
Total	\$ 1,469,026	\$ 1,426,219	\$ 1,559,674	\$ 1,575,741	\$ 1,498,073	\$ 18,435,724	\$ 25,964,457

OFF-BALANCE SHEET ARRANGEMENTS

FCRPS is not engaged in any off-balance sheet arrangements through unconsolidated limited purpose entities.

Critical accounting policies and estimates

Certain accounting policies require management to make estimates and judgments concerning transactions that will be settled in the future. Amounts recognized in the Financial Statements from such estimates are based upon numerous assumptions involving varying and potentially significant degrees of judgment and uncertainty. Accordingly, the amounts currently reflected in the Financial Statements will likely increase or decrease in the future as additional information becomes available.

REGULATORY ACCOUNTING POLICY

BPA's rates are designed to recover its cost of service. In connection with the rate-setting process, certain current costs or credits may be included in rates for recovery over future periods. Under those circumstances regulatory assets or liabilities are recorded in accordance with authoritative guidance for Regulated Operations. Such costs or credits are amortized either during the periods they are scheduled in rates or over the terms of the related nonfederal projects debt.

In order to defer incurred costs, 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. If BPA's rates should become market-based, any deferred costs and revenues would be expensed and recognized, respectively, in the Combined Statement of Revenues and Expenses in that period. Since BPA's rates are not structured to provide a rate of return on rate base assets, regulatory assets are recovered at cost without an additional rate of return. See Note 3, Effects of Regulation, for tables summarizing regulatory assets and liabilities as of Sept. 30, 2011, and 2010. Amortization of these assets and liabilities is reflected in the Combined Statements of Revenues and Expenses.

Quantitative and qualitative disclosures about risk

RISK MANAGEMENT

Due to the operational risk posed by fluctuations in river flows and electric market prices, net revenues that result from underlying surplus or deficit energy positions are inherently uncertain. BPA's Transacting Risk Management Committee has responsibility for the oversight of the market price, inventory and credit risks that arise from transacting in power markets. The TRMC establishes risk tolerances and limits that are represented in the transactional risk policy. This policy defines the control environment through which these risks are managed. Experienced business and risk analysts and managers conduct simulation and analysis of the hydro supply system and forward market prices to derive market price and credit risk positions. These results are measured against risk limits and reported to senior management. See Note 11, Risk Management and Derivative Instruments, for additional disclosure related to commodity, volumetric, credit and interest rate risk.

Non-GAAP financial information

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 Northwest Power and Conservation Council's Columbia River Basin Fish and Wildlife Program. Additionally, certain Columbia River Basin fish species are listed under the Endangered Species Act 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 U.S. Fish and Wildlife Service in furtherance of the ESA.

BPA's fish and wildlife costs consist of direct costs and operational impacts. Direct costs include integrated program costs. Operational impacts include replacement power purchase costs and estimated foregone power revenues. The following table includes these costs and estimates.

Fish and wildlife

Federal Columbia River Power System
For the years ended Sept. 30 (millions of dollars)

	2011	2010	2009
Direct costs	\$ 422	\$ 393	\$ 362
Operational impacts:			
Replacement power purchases	71	310	240
Estimated foregone power revenues	157	99	143
Total fish and wildlife	\$ 650	\$ 802	\$ 745

Federal Repayment

Revenue requirement study

The submission of BPA's annual report fulfills the reporting requirements of the Grand Coulee Dam - Third Powerplant Act, Public Law 89-448. The revenue requirement study demonstrates repayment of federal investment. It reflects revenues and costs consistent with BPA's 2010 Final Wholesale Power and Transmission Rate Proposal in July 2009 for fiscal years 2010 and 2011 (see WP-10-FS-BPA-02 and TR-10-FS-BPA-01). The final proposals filed with FERC contain the official amortization schedule for the rate periods. FERC approved the WP-10 and TR-10 filings on August 6, 2010.

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 FERC 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 operating and maintaining the power system.
2. Pay the cost of obtaining power through purchase and exchange agreements (nonfederal projects) that BPA is obtaining under capitalized lease-purchase agreements.
3. Pay interest on and repay outstanding U.S. Treasury borrowings 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 irrigation investment at federal reclamation projects assigned for payment from FCRPS power net revenues within the same period established for irrigation water users to repay their share of construction costs. 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

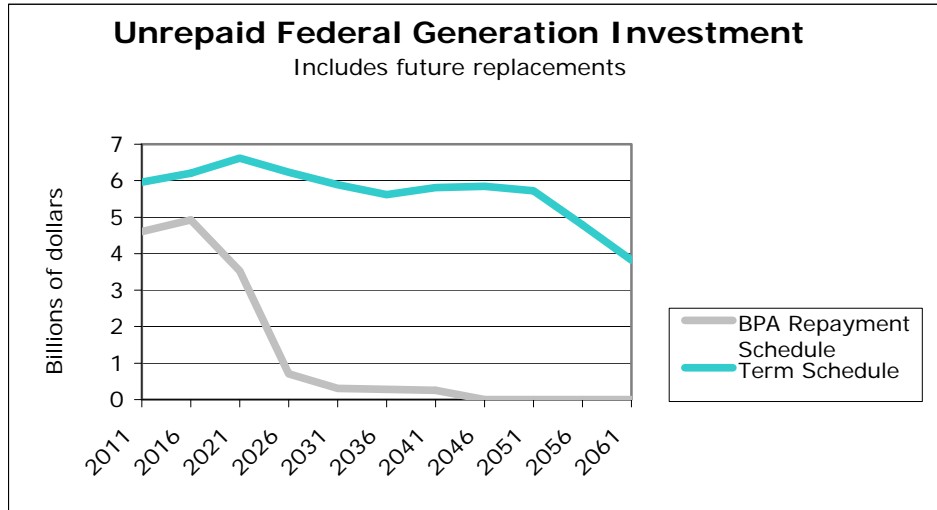
BPA's rates must be designed to collect sufficient revenues to return separately the power and transmission costs of each FCRPS investment and each irrigation assistance obligation within the time prescribed by law.

If existing rates are not likely to meet this requirement BPA must reduce costs, adjust its rates, or both. However, irrigation assistance payments from projects authorized subsequent to Public Law 89-448 are to be scheduled to not 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.

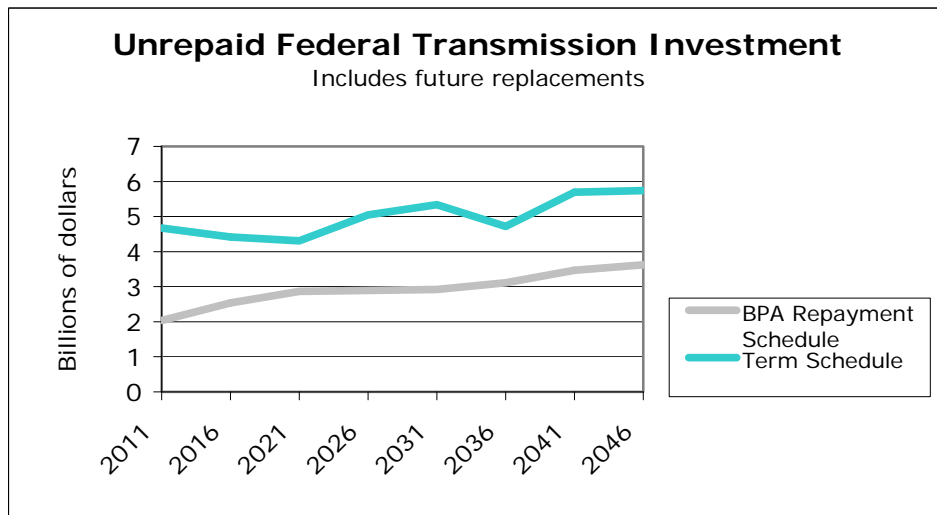
Reporting requirements of Public Law 89-448 are met so long as the unrepaid FCRPS investment and irrigation assistance resulting from BPA's repayment schedule are less than or equal to the allowable unrepaid investment in each year. While the comparison is illustrated here by graphs representing total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

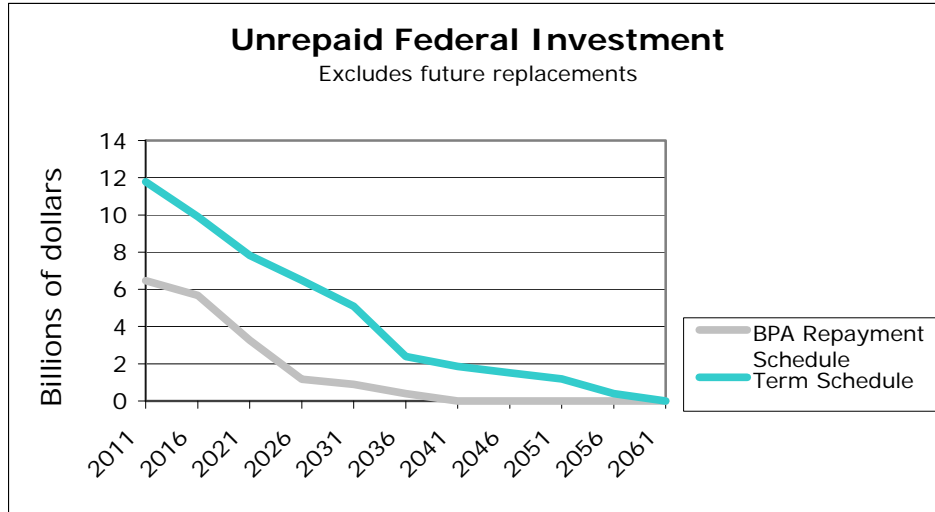


The term schedule lines in the graphs show how much of the obligation can remain unpaid in accordance with the repayment periods for the generation and transmission components of the FCRPS. The BPA repayment schedule lines show how much of the obligation remains to be repaid according to BPA's repayment 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 (35 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 2011 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.



www.bpa.gov

BONNEVILLE POWER ADMINISTRATION

DOE/BP-4366b • November 2011