

2011 Annual Report

Audited Financial Statements

Securing the Future



Audited Financial Statements

Table of Contents

Report of Independent Auditors.....	1
Financial Statements	2
Notes to Financial Statements.....	7





Report of Independent Auditors

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 revenues and expenses, of changes in capitalization and long-term liabilities and of cash flows present fairly, in all material respects, the financial position of the Federal Columbia River Power System (FCRPS) at September 30, 2011 and 2010, and the results of its operations and its cash flows for each of the three years in the period ended September 30, 2011, and the changes in its capitalization and long-term liabilities for each of the two years in the period ended September 30, 2011, in conformity with accounting principles generally accepted in the United States of America. These financial statements are the responsibility of the 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

October 27, 2011

Federal Columbia River Power System

Combined Balance Sheets

As of September 30

(Thousands of Dollars)

	2011	2010
Assets		
Utility plant		
Completed plant	\$ 14,741,720	\$ 14,362,387
Accumulated depreciation	(5,436,160)	(5,247,971)
	9,305,560	9,114,416
Construction work in progress	1,396,097	1,105,165
Net utility plant	10,701,657	10,219,581
Nonfederal generation	2,604,078	2,449,865
Current assets		
Cash and cash equivalents	892,125	1,078,671
Short-term investments in U.S. Treasury securities	253,348	65,783
Accounts receivable, net of allowance	119,596	122,400
Accrued unbilled revenues	207,089	197,603
Materials and supplies, at average cost	93,924	85,797
Prepaid expenses	29,430	25,832
Total current assets	1,595,512	1,576,086
Investments and other assets		
Regulatory assets	7,812,358	4,983,142
Investments in U.S. Treasury securities	39,129	82,328
Nonfederal nuclear decommissioning trusts	198,809	188,850
Deferred charges and other	223,736	169,318
Total investments and other assets	8,274,032	5,423,638
Total assets	\$ 23,175,279	\$ 19,669,170

The accompanying notes are an integral part of these statements.

Federal Columbia River Power System

Combined Balance Sheets

As of September 30

(Thousands of Dollars)

	2011	2010
Capitalization and Liabilities		
Capitalization and long-term liabilities		
Accumulated net revenues	\$ 2,510,373	\$ 2,428,691
Federal appropriations	4,324,881	4,238,167
Borrowings from U.S. Treasury	2,678,440	2,188,440
Nonfederal debt	5,843,046	6,015,585
Total capitalization and long-term liabilities	15,356,740	14,870,883
 Commitments and contingencies (Note 13)		
Current liabilities		
Federal appropriations	24,622	21,232
Borrowings from U.S. Treasury	265,000	325,000
Nonfederal debt	429,545	306,175
Accounts payable and other	523,459	613,052
Total current liabilities	1,242,626	1,265,459
 Other liabilities		
Regulatory liabilities	2,456,343	2,494,019
IOU exchange benefits	3,161,251	85,017
Asset retirement obligations	176,212	170,334
Deferred credits and other	782,107	783,458
Total other liabilities	6,575,913	3,532,828
 Total capitalization and liabilities	 \$ 23,175,279	 \$ 19,669,170

The accompanying notes are an integral part of these statements.

Federal Columbia River Power System

Combined Statements of Revenues and Expenses

For the Years Ended September 30

(Thousands of Dollars)

	2011	2010	2009
Operating revenues			
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	65,463	66,144	62,692
Total operating revenues	3,284,774	3,055,131	2,870,284
Operating expenses			
Operations and maintenance	1,734,306	1,589,171	1,578,421
Purchased power	177,953	381,468	317,543
Nonfederal projects	624,972	600,360	501,367
Depreciation and amortization	393,502	368,371	355,574
Total operating expenses	2,930,733	2,939,370	2,752,905
Net operating revenues	354,041	115,761	117,379
Interest expense and (income)			
Interest expense	352,904	331,255	326,494
Allowance for funds used during construction	(42,983)	(32,867)	(30,710)
Interest income	(37,562)	(55,046)	(77,355)
Net interest expense	272,359	243,342	218,429
Net revenues (expenses)	81,682	(127,581)	(101,050)
Accumulated net revenues at October 1	2,428,691	2,556,272	2,664,460
Irrigation assistance	-	-	(7,138)
Accumulated net revenues at September 30	\$ 2,510,373	\$ 2,428,691	\$ 2,556,272

The accompanying notes are an integral part of these statements.

Federal Columbia River Power System

Combined Statements of Changes in Capitalization and Long-Term Liabilities

Including Current Portions

(Thousands of Dollars)

Balance at September 30	Accumulated Net Revenues	Federal Appropriations	Borrowings from U.S. Treasury	Nonfederal Debt	Total
2009	\$ 2,556,272	\$ 4,396,189	\$ 2,130,440	\$ 6,564,934	\$ 15,647,835
Federal appropriations:					
Proceeds	-	68,039	-	-	68,039
Repayment	-	(204,829)	-	-	(204,829)
Borrowings from U.S. Treasury:					
Proceeds	-	-	638,000	-	638,000
Repayment	-	-	(255,000)	-	(255,000)
Nonfederal debt:					
Proceeds	-	-	-	27,351	27,351
Repayment	-	-	-	(270,525)	(270,525)
Net expenses	(127,581)	-	-	-	(127,581)
2010	\$ 2,428,691	\$ 4,259,399	\$ 2,513,440	\$ 6,321,760	\$ 15,523,290
Federal appropriations:					
Proceeds	-	129,632	-	-	129,632
Repayment	-	(39,528)	-	-	(39,528)
Borrowings from U.S. Treasury:					
Proceeds	-	-	800,000	-	800,000
Repayment	-	-	(370,000)	-	(370,000)
Nonfederal debt:					
Proceeds	-	-	-	349,108	349,108
Extinguished through refinancing	-	-	-	(90,000)	(90,000)
Repayment	-	-	-	(308,277)	(308,277)
Net revenues	81,682	-	-	-	81,682
2011	\$ 2,510,373	\$ 4,349,503	\$ 2,943,440	\$ 6,272,591	\$ 16,075,907

The accompanying notes are an integral part of these statements.

Federal Columbia River Power System

Combined Statements of Cash Flows

For the Years Ended September 30

(Thousands of Dollars)

	2011	2010	2009
Cash provided by and (used for) operating activities			
Net revenues (expenses)	\$ 81,682	\$ (127,581)	\$ (101,050)
Non-cash items:			
Depreciation and amortization	393,502	368,371	355,574
Amortization of nonfederal projects	306,175	270,525	189,882
Unrealized (gain) loss on derivative instruments	-	(14,800)	34,706
Changes in:			
Receivables and unbilled revenues	(5,112)	(30,109)	32,561
Materials and supplies	(8,127)	(8,185)	(1,893)
Prepaid expenses	(3,598)	(1,180)	(2,970)
Accounts payable and other	(50,229)	91,915	(138,548)
Regulatory assets and liabilities	(209,173)	(164,775)	35,897
Other assets and liabilities	(68,134)	(13,813)	(135,690)
Net cash provided by operating activities	436,986	370,368	268,469
Cash provided by and (used for) investing activities			
Investment in:			
Utility plant (including AFUDC)	(787,384)	(683,680)	(575,083)
U.S. Treasury Securities:			
Purchases	(310,000)	(100,000)	(110,000)
Maturities	163,193	44,683	9,891
Deposits to nonfederal nuclear decommissioning trusts	(9,616)	(8,753)	(8,211)
Special purpose corporations' trust funds:			
Deposits to	(106,260)	(4,646)	(199,916)
Receipts from	66,601	39,780	108,081
Net cash used for investing activities	(983,466)	(712,616)	(775,238)
Cash provided by and (used for) financing activities			
Federal appropriations:			
Proceeds	129,632	86,470	176,887
Repayment	(39,528)	(204,829)	(38,559)
Borrowings from U.S. Treasury:			
Proceeds	800,000	638,000	338,000
Repayment	(370,000)	(255,000)	(393,460)
Nonfederal debt:			
Proceeds	201,963	4,646	199,916
Extinguished through refinancing	(90,000)	-	-
Repayment	(308,277)	(270,525)	(189,882)
Customers:			
Advances for construction	59,806	92,786	63,492
Reimbursements to customers	(23,662)	(27,648)	(16,706)
Irrigation assistance paid	-	-	(7,138)
Net cash provided by financing activities	359,934	63,900	132,550
Net decrease in cash and cash equivalents	(186,546)	(278,348)	(374,219)
Cash and cash equivalents at beginning of year	1,078,671	1,357,019	1,731,238
Cash and cash equivalents at end of year	\$ 892,125	\$ 1,078,671	\$ 1,357,019
Supplemental disclosures:			
Cash paid for interest, net of amount capitalized	\$ 375,755	\$ 360,813	\$ 362,305
Significant noncash investing and financing activities:			
Accrued capital expenditures increase	\$ 43,586	\$ 46,247	\$ 33,328
Federal appropriations write-off	\$ -	\$ (18,431)	\$ -
Nonfederal debt increase for Energy Northwest	\$ 147,145	\$ 22,705	\$ 88,028

The accompanying notes are an integral part of these statements.

Notes to Financial Statements

1. Summary of Significant Accounting Policies

ACCOUNTING PRINCIPLES

Combination and consolidation of entities

The Federal Columbia River Power System (FCRPS) financial statements combine the accounts of the Bonneville Power Administration (BPA), the accounts of the Pacific Northwest generating facilities of the U.S. Army Corps of Engineers (Corps) and the Bureau of Reclamation (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 (NIFCs), from which BPA leases certain transmission facilities. (See Note 8, Nonfederal Financing.)

BPA is the power marketing administration that purchases, transmits and markets power for the FCRPS. Each of the combined entities is separately managed and financed, but the facilities are operated as an integrated power system with the financial results combined as the FCRPS. While the costs of Corps and Reclamation projects serve multiple purposes, only the power portion of total project costs are assigned to the FCRPS through a cost allocation process. All intracompany and intercompany accounts and transactions have been eliminated from the combined financial statements.

FCRPS accounts are maintained in accordance with generally accepted accounting principles of the United States of America 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 directives issued by U.S. government agencies. BPA is a separate and distinct entity within the U.S. Department of Energy; Reclamation and U.S. Fish and Wildlife Service 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.

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.

Rates and regulatory authority

BPA establishes separate power and transmission rates in accordance with several statutory directives. Rates proposed by BPA are subject to an extensive formal hearing 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 out by the Energy Policy Act of 1992, 16 U.S.C. 824. Statutory standards include a requirement that these rates be sufficient to ensure 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 are subject to review by the United States 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.

In accordance with authoritative guidance for Regulated Operations, certain costs or credits may be included in rates for recovery or refund over a future period and are recorded as regulatory assets or liabilities. (See Note 3, Effects of Regulation.) Regulatory assets or liabilities are amortized over the periods they are included in rates. Costs are recovered through rates during the periods when the costs are scheduled to be repaid. Amortization

is computed using either the straight-line method or is based upon specific amounts included in rates each year. 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.

Utility plant

Utility plant is stated at original cost and includes generation and transmission assets. Generation assets were \$7.96 billion and \$7.76 billion, and transmission assets were \$6.78 billion and \$6.60 billion at Sept. 30, 2011, and 2010, respectively. The costs of substantial additions, major replacements and substantial betterments are capitalized. 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. Maintenance, repairs and replacements of items determined to be less than major units of property are charged to maintenance and operating expense as incurred. When BPA retires utility plant, it charges the original cost and any net proceeds from the disposition to accumulated depreciation.

Depreciation

Depreciation of the original cost of generation plant is computed using straight-line methods based on estimated service lives of the various classes of property, which average 75 years. For transmission plant, depreciation of original cost and estimated net cost of removal is computed primarily on the straight-line group life method based on estimated service lives of the various classes of property, which average 40 years. The net cost of removal is included in depreciation; however, in the event there is negative salvage, a reclassification of the negative salvage reserve not associated with asset retirement obligations is made from accumulated depreciation to a regulatory liability.

Allowance for funds used during construction

Allowance for funds used during construction (AFUDC) represents the estimated cost of interest on financing the construction of new assets. AFUDC is based on the construction work in progress balance and is charged to the capitalized cost of the utility plant asset. AFUDC is a non-cash reduction of interest expense.

FCRPS capitalizes AFUDC at one rate for Corps and Reclamation construction funded by congressional appropriations and at another rate for construction funded substantially by BPA and the NIFCs. The rates for appropriated funds are provided each year to BPA by the U.S. Treasury, whereas the BPA rate is determined based on the weighted-average cost of borrowing for BPA and the NIFCs. The respective rates were approximately 0.3 percent and 4.4 percent in fiscal year 2011, 0.4 percent and 4.8 percent in fiscal year 2010, and 2.0 percent and 5.2 percent in fiscal year 2009.

Nonfederal generation

BPA has acquired all of the generating capability of Energy Northwest's Columbia Generating Station (CGS) nuclear power plant. The contracts to acquire the generating capability of the project require BPA to cover all of CGS's operating, maintenance and debt service costs. BPA also has acquired all of the output of the Lewis County PUD's Cowlitz Falls Hydroelectric Project and pays all related operating, maintenance and debt service costs. BPA recognizes expenses for these projects based upon total project cash funding requirements. The nonfederal generation assets in the Combined Balance Sheets are amortized over the term of the outstanding debt. (See Note 8, Nonfederal Financing.)

Cash and cash equivalents

Cash amounts include cash in the BPA fund with the U.S. Treasury and unexpended appropriations of the Corps and Reclamation. Cash equivalents represent short-term U.S. Treasury market-based special securities with maturities of 90 days or less at the date of investment. (See Note 2, Investments in U.S. Treasury Securities.) The carrying value of cash and cash equivalents approximates fair value.

Concentrations of credit risks

General credit risk

Financial instruments that 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 receivable are spread across a diverse group of consumer-owned utilities (COUs), investor-owned utilities (IOUs), power marketers, wind generators and others that are located throughout the western United States and Canada. The accounts receivable exposure results 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 years 2011, 2010 and 2009, 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. In order to further manage credit risk, BPA obtains credit support, such as letters of credit, parental guarantees, cash in the form of prepayment and deposit or escrow from some counterparties. BPA closely monitors counterparties for changes in financial condition and regularly updates credit reviews.

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 customer accounts, based upon the best available facts and circumstances of customers that may be unable to meet their financial obligations, and a reserve for all other customers based on historical experience.

The largest risk relates to the California power markets that were in turmoil during 2000 to 2001 when they experienced historically high power prices and volatility, along with continued uncertainty related to deregulation. The California Independent System Operator and California Power Exchange were customers with whom BPA had contracts for power and transmission delivery during that period, and they have not fully paid BPA for their purchases. (See Note 13, Commitments and Contingencies.) BPA has recorded an allowance for these accounts, which in management's best estimate is sufficient to cover potential exposure. Net exposure after this allowance is not significant. BPA has continued to pursue collection of amounts due.

Derivative instruments

BPA follows the Derivatives and Hedging accounting guidance that requires every derivative instrument be recorded on the balance sheet as an asset or liability measured at its fair value and also requires that a 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 purchases and normal sales exception under the Derivatives and Hedging accounting guidance. Forward electricity contracts are generally considered normal purchases and normal sales if they require physical delivery, are expected to be used or sold by BPA in the normal course of business and meet the definition of capacity described in the Derivatives and Hedging accounting guidance. These transactions are not required to be recorded at fair value in the financial statements. Recognition of these contracts in Sales or Purchased power in the Combined Statements of Revenues and Expenses occurs when the contracts settle.

In fiscal year 2010, BPA began applying Regulated Operations accounting treatment to its derivative instruments that do not qualify for the normal purchases and normal sales exception and are recorded at fair value. As such, unrealized gains or losses associated with these derivative instruments are recorded on the Combined Balance Sheets under Regulatory assets or Regulatory liabilities.

Fair value

BPA's carrying amounts of current assets and current liabilities approximates fair value based on the short-term nature of these instruments. In accordance with authoritative guidance for Fair Value Measurements and Disclosures, BPA uses fair value measurements to record adjustments to certain financial assets and liabilities and to determine fair value disclosures. When developing fair value measurements, it is BPA's policy to use quoted market prices whenever available or to maximize the use of observable inputs and minimize the use of unobservable inputs when quoted market prices are not available. Fair values are primarily developed using industry standard models that consider various inputs including: (a) quoted forward prices for commodities; (b) time value; (c) volatility factors; (d) current market and contractual prices for underlying instruments; (e) market interest rates and yield curves; and (f) credit spreads, as well as other relevant economic measures. (See Note 11, Risk Management and Derivative Instruments and Note 12, Fair Value Measurements.)

Revenues and net revenues

Operating revenues are recorded when services are rendered and include estimated unbilled revenues. BPA's net revenues over time are committed to repayment of the U.S. government investment in the FCRPS, the payment of certain irrigation costs and the payment of operational obligations, including debt for both operating and nonoperating nonfederal projects. (See Note 13, Commitments and Contingencies.)

Interest income

Interest income includes interest earned on BPA's fund balance with the U.S. Treasury and interest earned on investments in market-based special securities. BPA earns interest on cash balances in the fund at the weighted-average interest rate of its outstanding U.S. Treasury borrowings and reduces its monthly debt interest payments by the interest earned. Interest earnings on investments are based on the stated rates of the individual market-based special securities.

U.S. Treasury credits for fish

The Northwest Power Act obligates the BPA administrator to make expenditures for fish and wildlife protection, mitigation and enhancement for both power and nonpower purposes on a reimbursement basis. The Northwest Power Act also specifies 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. Power related costs are recovered in BPA's rates. Nonpower related costs are recovered as a reduction to BPA's cash payment to the U.S. Treasury.

Residential Exchange Program

In order to provide qualifying regional utilities, primarily IOUs, access to benefits from the FCRPS, Congress established the Residential Exchange Program (REP) in Section 5(c) of the Northwest Power Act. Whenever a Pacific Northwest electric utility offers to sell power to BPA at the utility's average system cost of resources, BPA purchases such power and offers, in exchange, to sell an equivalent amount of power at BPA's priority firm exchange rate to the utility for resale to that utility's residential and small farm consumers. REP costs are forecast for each year of the rate period and included in the revenue requirement for establishing rates. The cost of this program is collected through rates with program costs recognized when incurred net of the purchase and sale of power under the REP.

In fiscal year 2008, BPA conducted the 2007 Supplemental Wholesale Power Rate Case (WP-07 Supplemental Rate Case) to resolve outstanding claims and address associated judicial rulings related to prior REP billings. In 2009, BPA conducted the 2010 Wholesale Power and Transmission Rate Adjustment Proceeding (WP-10 Rate Case), continuing the policies established in WP-07 Supplemental Rate Case. In connection with those filings, Lookback Amounts due to and due from BPA customers were identified and recorded as regulatory amounts. Such Lookback Amounts were collected from identified IOU customers and were being returned to the COUs over time.

In fiscal year 2011, the BPA administrator signed the 2012 Residential Exchange Program Settlement Agreement (Settlement Agreement), resolving disputes related to the REP. The Settlement Agreement provides for fixed “Scheduled Amounts” payable to the IOUs, as well as fixed “Refund Amounts” payable to the COUs. The Settlement Agreement eliminates the Lookback Amounts as of Sept. 30, 2011, but replaces them with the Refund Amounts for amounts overpaid by the COUs. These amounts do not reduce rates, but are reflected as credits to qualifying COUs’ bills as designated in the Settlement Agreement. BPA utilizes the rates process to reduce the IOUs’ benefits and thus reduce expense in the year it is applied. These transactions are net operating revenue neutral as the same amount reduces both revenue and expense. (See Note 9, Residential Exchange Program.)

RECENT ACCOUNTING PRONOUNCEMENTS

Receivables

In July 2010, the Financial Accounting Standards Board (FASB) issued authoritative guidance requiring new disclosures about the credit quality of certain financing receivables, as well as the related allowances for credit losses. The required disclosures are intended to facilitate financial statement users’ evaluation of the nature of credit risk inherent in an entity’s portfolio of financing receivables, how that risk is assessed and analyzed in arriving at the allowance for credit losses and the reasons for those changes in the allowance for credit losses. The disclosures are required to be made on a disaggregated basis and include qualitative and quantitative information about financing receivables, the allowance for credit losses, impaired balances and credit quality indicators. This guidance will be effective for fiscal year 2012. BPA is determining the extent to which financing receivables guidance is, or will be, relevant to BPA and the potential related impact on BPA’s financial statements.

Fair value measurements and disclosures

In January 2010, the FASB issued authoritative guidance related to fair value disclosures. The guidance requires additional detailed disclosure for all levels of fair value measurements. The amounts of significant transfers in and out of Levels 1 and 2 are required to be disclosed, along with the reasons for those transfers. Purchase, issuance and settlement activity in Level 3 is required to be disclosed on a gross basis. Fair value measurement disclosures are required for each class of assets and liabilities. These classes are a matter of management judgment. The guidance further requires disclosures about inputs and valuation techniques used for both Level 2 and Level 3 fair value measurements. This guidance became effective fiscal year 2011 with the exception of the gross disclosure of purchase, issuance and settlement activity in Level 3, which will be effective in fiscal year 2012. BPA adopted this guidance (with the exception of that relating to the gross disclosure of purchase, issuance and settlement activity in Level 3) on Oct. 1, 2010, with no material impact on its financial condition, results of operations or cash flows. BPA does not expect any significant impact from the guidance for the gross disclosure of purchase, issuance and settlement activity in Level 3 on BPA’s financial statements.

In May 2011, the FASB issued authoritative guidance which made a number of incremental changes to current fair value measurement and disclosure guidance. Changes with potential relevance to BPA include the clarification of the concept of “highest and best use” in fair value measurements, guidance on when financial instruments may be recorded on a net basis, and certain additional required disclosures for fair value measurements. The guidance will be effective for fiscal year 2012. BPA is evaluating the impact on BPA’s financial statements.

Variable interest entities

In June 2009, the FASB issued authoritative guidance that updated and amended consolidation accounting standards. The accounting standards update replaced the quantitative approach for determining who has the controlling financial interest in a variable interest entity (VIE) with a qualitative approach and requires ongoing assessments of an entity’s relationship with a VIE. BPA adopted this guidance on Oct. 1, 2010. The adoption of this guidance had no impact to BPA’s financial condition, results of operations or cash flows.

A VIE is an entity that does not have sufficient equity at risk to finance its activities without additional subordinated financial support from other parties or whose equity investors lack any characteristics of a controlling financial interest. An entity has a controlling financial interest if it has the obligation to absorb expected losses or receive expected gains that could potentially be significant to a VIE and the power to direct the activities that are most significant to a VIE's economic performance. An enterprise that has a controlling financial interest is known as the VIE's primary beneficiary and is required to consolidate the VIE.

BPA conducted a detailed review and analysis of agreements with counterparties that may be considered VIEs under this new standard. BPA determined it may transact with VIEs when it executes power purchase agreements. These VIEs are typically legal entities structured to own and operate specific generating facilities, primarily wind farms. The power purchase agreements could lead to BPA having a variable interest in the VIE if the agreements provide that BPA absorb risk from the perspective of the VIE. BPA has a number of power purchase agreements, which, because of their pricing arrangements, provide that BPA absorb commodity price risk of the counterparty entities. BPA does not provide, and does not plan to provide, any additional financial support to these entities beyond what BPA is contractually obligated to pay. BPA has concluded that in no instance does it have the power to control the most significant activities of these entities as the result of a power purchase agreement, and, as such, in no instance is BPA the primary beneficiary. BPA does not have control over the operating and maintenance activities that most significantly impact these entities. As a result of this review, BPA has not recorded any assets or liabilities related to the power purchase agreements with these entities and BPA has not consolidated any entities because of power purchase agreements.

BPA also reviewed the arrangements with the five NIFC entities and determined that BPA remains the primary beneficiary of these VIEs. BPA therefore continues to consolidate the NIFC entities into the FCRPS financial statements. (See Note 8, Nonfederal Financing.)

SUBSEQUENT EVENTS

FCRPS has performed an evaluation of events and transactions for potential recognition or disclosure through Oct. 27, 2011, which is the date the financial statements were issued.

2. Investments in U.S. Treasury Securities

<i>As of Sept. 30 — thousands of dollars</i>	2011		2010	
	Amortized cost	Fair value	Amortized cost	Fair value
Short-term	\$ 253,348	\$ 253,656	\$ 65,783	\$ 66,090
Long-term	39,129	40,712	82,328	85,132
Total	\$ 292,477	\$ 294,368	\$ 148,111	\$ 151,222

In fiscal year 2009, BPA began participating in the U.S. Treasury's Federal Investment Program. Through this program, the U.S. Treasury provides investment services to federal government entities that have funds on deposit with the U.S. Treasury and have legislative authority to invest those funds. Investments of the funds are generally restricted to special non-marketable securities, also called market-based specials. Under its banking arrangement with the U.S. Treasury, BPA has agreed to invest \$100 million annually for up to 10 years or until the BPA fund is fully invested. Any remaining balance in the BPA fund at the 10th year will be invested through the Federal Investment Program.

Market-based specials held during fiscal years 2011 and 2010 had a weighted-average yield of 0.8 percent and 1.3 percent, respectively, and maturities of up to five years. The amounts shown in the table above exclude

U.S. Treasury securities with maturities of 90 days or less at the date of investment, which are considered cash equivalents and are included in the Combined Balance Sheets as part of Cash and cash equivalents. For all other securities, BPA follows the authoritative guidance for Investments, Debt and Equity Securities. These investments are classified as held-to-maturity and reported at amortized cost. Investments with maturities that will be realized in cash within one year are classified as short-term investments. Long-term investments have stated maturities between one and three years from the balance sheet date.

3. Effects of Regulation

REGULATORY ASSETS

<i>As of Sept. 30 — thousands of dollars</i>	2011	2010
REP Scheduled Amounts	\$ 3,074,870	\$ —
Terminated nuclear facilities	2,986,393	3,377,550
REP Refund Amounts	565,359	—
Columbia River Fish Mitigation	469,783	436,912
Conservation measures	272,924	171,233
Fish and wildlife measures	246,480	180,256
Settlements	50,428	49,828
Federal Employees' Compensation Act	31,352	29,945
Derivative instruments	27,422	51,563
Trojan decommissioning and site restoration	23,506	24,152
Spacer damper replacement program	21,853	35,995
Terminated hydro facilities	21,740	22,785
Capital bond premiums	10,554	11,431
Sponsored conservation	8,615	21,865
REP Lookback Amount from IOUs	—	568,542
Other	1,079	1,085
Total	\$ 7,812,358	\$ 4,983,142

Regulatory assets include the following items:

“REP Scheduled Amounts” reflect the costs of future REP Scheduled Amounts representing REP benefits payable under the 2012 REP Settlement Agreement that will be recovered through rates. (See Note 9, Residential Exchange Program.)

“Terminated nuclear facilities” include the nonfederal debt for Energy Northwest Nuclear Project Nos. 1 and 3. These assets are amortized over the term of the related outstanding debt. (See Note 8, Nonfederal Financing.)

“REP Refund Amounts” is the amount recoverable in future rate periods that reduces the REP benefit payments. These costs will be recovered through future rates as reductions to IOU REP benefits as established in the 2012 REP Settlement Agreement. (See Note 9, Residential Exchange Program.)

“Columbia River Fish Mitigation” is the cost of research and development for fish bypass facilities funded through appropriations since 1989 in accordance with the Energy and Water Development Appropriations Act of 1989, Public Law 100-371. These costs are recovered through rates and amortized as scheduled over 75 years.

“Conservation measures” consist of the costs of capitalized conservation measures and are amortized over periods from five to 20 years.

“Fish and wildlife measures” consist of capitalized fish and wildlife projects and are amortized over a period of 15 years.

“Settlements” reflect costs related to settlement agreements resulting from litigation. These costs will be recovered and amortized through future rates over a period as established by the administrator.

“Federal Employees’ Compensation Act” reflects the actuarial estimated amount of future payments for current recipients of BPA’s worker compensation benefits.

“Derivative instruments” reflects the unrealized losses from BPA’s derivative instruments that are marked-to-market in accordance with current authoritative derivative accounting guidance. (See Note 11, Risk Management and Derivative Instruments.) These amounts are deferred over the corresponding underlying contract delivery months.

“Trojan decommissioning and site restoration” costs reflect the amount to be recovered in future rates for funding the Trojan asset retirement obligation (ARO) liability. (See Note 4, Asset Retirement Obligations.)

“Spacer damper replacement program” consists of costs to replace deteriorated spacer dampers that have been deferred and are being recovered in rates under the Spacer Damper Replacement Program. These costs are being amortized over a period of 30 years. In fiscal year 2011, BPA recognized an impairment charge of \$20.6 million in deferred spacer damper replacement program costs.

“Terminated hydro facilities” include the nonfederal debt for the terminated Northern Wasco hydro project. These assets are amortized as the principal on the outstanding debt is repaid.

“Capital bond premiums” are losses related to refinanced debt and are amortized over the life of the new debt instruments.

“Sponsored conservation” relates to the nonfederal debt for Conservation and Renewable Energy System (CARES) and City of Tacoma Conservation bonds. These were issued to finance conservation programs sponsored by BPA. The assets are amortized as the principal on the outstanding debt is repaid.

“REP Lookback Amount from IOUs” is the amount that was recoverable from IOUs in future rate periods that reduces their REP benefit payments. This regulatory asset was eliminated with the 2012 REP Settlement Agreement. (See Note 9, Residential Exchange Program.)

REGULATORY LIABILITIES

<i>As of Sept. 30 — thousands of dollars</i>	2011	2010
Capitalization adjustment	\$ 1,601,796	\$ 1,666,701
REP Refund Amounts to COUs	565,359	—
Accumulated plant removal costs	201,266	186,764
CGS decommissioning and site restoration	51,409	48,530
Derivative instruments	30,924	17,701
REP Lookback Amount to COUs	—	568,542
Other	5,589	5,781
Total	\$ 2,456,343	\$ 2,494,019

Regulatory liabilities include the following items:

“Capitalization adjustment” is the difference between appropriated debt before and after refinancing per the BPA Refinancing Section of the Omnibus Consolidated Rescissions and Appropriations Act of 1996 (Refinancing Act), 16 U.S.C. 838(l). The 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 for fiscal years 2011, 2010 and 2009, respectively. (See Note 6, Federal Appropriations.)

“REP Refund Amounts to COUs” is the amount previously collected through rates that is owed qualifying consumer-owned utilities and will be credits on their future bills. These costs will be repaid and amortized through future rates over a period as established in the 2012 REP Settlement Agreement. (See Note 9, Residential Exchange Program.)

“Accumulated plant removal costs” is the amount previously collected through rates as part of depreciation. These costs will be relieved as actual removal costs are paid.

“CGS decommissioning and site restoration” is the amount previously collected through rates in excess of the ARO balances for CGS decommissioning and site restoration as well as Project Nos. 1 and 4 sites.

“Derivative instruments” reflects the unrealized gains from BPA's derivative instruments that are marked-to-market in accordance with current authoritative derivative accounting guidance. (See Note 11, Risk Management and Derivative Instruments.) These amounts are deferred over the corresponding underlying contract delivery months.

“REP Lookback Amount to COUs” is the amount that was previously collected through rates that is owed qualifying consumer-owned utilities and will be credits on their future bills. This regulatory liability was eliminated with the 2012 REP Settlement Agreement. (See Note 9, Residential Exchange Program.)

4. Asset Retirement Obligations

<i>As of Sept. 30 — thousands of dollars</i>	2011	2010
Beginning Balance	\$ 170,334	\$ 162,943
Activities:		
Accretion	8,640	8,324
Expenditures	(2,234)	(1,806)
Revisions	(528)	873
Ending Balance	\$ 176,212	\$ 170,334

BPA recognizes AROs according to the estimated fair value of the dismantlement and restoration costs associated with the retirement of certain tangible long lived assets. The liability is adjusted for any revisions, expenditures and the passage of time. FCRPS also has tangible long lived assets such as federal hydro projects without an associated ARO since no future obligation exists to remove these projects.

ARO include the following items as of Sept. 30, 2011:

- CGS decommissioning and site restoration of \$133.3 million;
- Trojan decommissioning of \$23.5 million;
- Energy Northwest Project Nos. 1 and 4 site restoration of \$16.1 million;
- BPA owned transmission assets of \$3.3 million.

NONFEDERAL NUCLEAR DECOMMISSIONING TRUSTS

<i>As of Sept. 30 — thousands of dollars</i>	2011		2010	
	Amortized cost	Fair value	Amortized cost	Fair value
U.S. government obligation mutual funds	\$ 84,050	\$ 86,834	\$ 101,142	\$ 105,999
Equity index funds	77,097	74,923	77,413	80,867
Corporate bond index funds	36,834	37,028	1,949	1,954
Cash and cash equivalents	24	24	30	30
Total	\$ 198,005	\$ 198,809	\$ 180,534	\$ 188,850

BPA recognizes an asset that represents trust fund balances for decommissioning and site restoration costs. Decommissioning costs for CGS are charged to operations over the operating life of the project. External trust funds for decommissioning and site restoration costs are 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 the Nuclear Regulatory Commission (NRC) requirements. The NRC requires that this period be no longer than 60 years from the time the plant stops operating. The plant is licensed to operate until the current operating license termination year of 2024. Trust fund requirements for CGS are based on an NRC decommissioning cost estimate and the license termination date. The trusts are funded and managed by BPA in accordance with the NRC requirements and site certification agreements.

The investment securities in the decommissioning and site restoration trust are classified by BPA as available-for-sale in accordance with accounting guidance related to Investments, Debt and Equity Securities. Payments to the trusts for fiscal years 2011, 2010 and 2009 were approximately \$9.6 million, \$8.8 million and \$8.2 million, respectively.

Based on an agreement in place BPA directly funds Eugene Water and Electric Board's 30 percent share of Trojan's decommissioning costs through current rates. Decommissioning costs are included in Operations and maintenance expense in the accompanying Combined Statements of Revenues and Expenses.

5. Deferred Charges and Other

<i>As of Sept. 30 — thousands of dollars</i>	2011	2010
Special purpose corporations' trust funds	\$ 155,301	\$ 117,212
Derivative instruments	32,380	20,682
Spectrum Relocation fund	15,884	23,603
Trust fund and other deposits	11,341	639
Energy receivable	5,334	3,953
Other	3,496	3,229
Total	\$ 223,736	\$ 169,318

Deferred charges and other include the following items:

"Special purpose corporations' trust funds" are amounts held in separate trust accounts for the construction of transmission assets, debt service payments during the construction period and a fund mainly for future principal and interest debt service payments. (See Note 8, Nonfederal Financing.)

"Derivative instruments" represent unrealized gains from the derivative portfolio which includes physical power purchase and sale transactions, power exchange transactions, and power and heat rate option contracts.

The Commercial Spectrum Enhancement Act created the "Spectrum Relocation fund" to reimburse the costs of replacing radio communication equipment displaced as a result of radio band frequencies no longer available to federal agencies. Amounts received from the U.S. Treasury in connection with the Act are held in the BPA fund and are restricted for use in constructing replacement assets.

"Trust fund and other deposits" primarily represents funds held in the CARES defeasance trust fund.

"Energy receivable" primarily consists of energy to be returned to BPA for prior transmission line losses.

6. Federal Appropriations

Appropriations consist primarily of the power portion of Corps and Reclamation capital investments funded through congressional appropriations and the remaining unpaid capital investments in the BPA transmission

system, which were made prior to implementation of the Federal Columbia River Transmission System Act of 1974, 16 U.S.C. 838(j).

The Refinancing Act required that the outstanding balance of the FCRPS federal appropriations be reset and assigned market rates of interest prevailing as of Oct. 1, 1996. This resulted in a determination that the principal amount of appropriations should 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. Appropriations in the amount of \$6.69 billion were subsequently refinanced for \$4.10 billion. This adjustment was recorded as a capitalization adjustment in regulatory liabilities and is being amortized over the remaining period of repayment. (See Note 3, Effects of Regulation.)

Federal generation and transmission appropriations are repaid to the U.S. Treasury within the weighted-average service lives of the associated investments from the time each facility was placed in service, with a maximum of 50 years. Federal appropriations may be paid early without penalty.

The weighted-average interest rate was 6.3 percent and 6.4 percent on outstanding appropriations as of Sept. 30, 2011, and 2010, respectively.

MATURING FEDERAL APPROPRIATIONS

As of Sept. 30 — thousands of dollars

2012	\$	24,622
2013		18,250
2014		19,198
2015		54,788
2016		—
2017 and thereafter		4,232,645
Total	\$	4,349,503

7. Borrowings from U.S. Treasury

BPA is authorized by Congress to issue to the U.S. Treasury and have outstanding at any one time, up to \$7.70 billion of interest bearing debt with terms and conditions comparable to debt issued by U.S. government corporations. The debt may be issued to finance BPA's capital programs, which include Corps and Reclamation direct funded capital investments. Of the \$7.70 billion, \$750 million can be issued to finance Northwest Power Act related expenses and \$1.25 billion is restricted for conservation and renewable resources.

At Sept. 30, 2011, of the total \$2.94 billion of outstanding bonds, \$252.8 million were conservation and renewable resources investments. There were no outstanding bonds with variable rates of interest at Sept. 30, 2011. At Sept. 30, 2010, \$45.0 million of outstanding bonds carried a variable interest rate. The weighted-average interest rate of BPA's borrowings from the U.S. Treasury exceeds current rates. As a result, the fair value of BPA's U.S. Treasury borrowings exceeded the carrying value by approximately \$462.6 million and \$323.7 million, based on discounted future cash flows using agency rates offered by the U.S. Treasury as of Sept. 30, 2011, and 2010, respectively, for similar maturities.

The weighted-average interest rate on outstanding U.S. Treasury borrowings was 4.2 percent and 4.4 percent as of Sept. 30, 2011, and 2010, respectively. At Sept. 30, 2010, the outstanding bonds with a variable rate of interest carried an interest rate of 0.2 percent.

U.S. Treasury borrowings of \$2.47 billion are callable by BPA through Jan. 31, 2014. Of this amount, \$35.0 million is callable at 100 percent of the principal value and the remainder is callable at a premium or discount, which is calculated based on the current government agency rates for the remaining term to maturity at the time the bond is called.

MATURING BORROWINGS FROM U.S. TREASURY

As of Sept. 30 — thousands of dollars

2012	\$	265,000
2013		122,800
2014		103,000
2015		80,000
2016		30,000
2017 through 2039		2,342,640
Total	\$	2,943,440

8. Nonfederal Financing

PROJECTS FINANCED WITH NONFEDERAL DEBT

As of Sept. 30 — thousands of dollars

	2011	2010
Terminated nuclear facilities:		
Nuclear Project No. 1	\$ 1,573,805	\$ 1,739,835
Nuclear Project No. 3	1,495,480	1,637,715
Terminated nuclear facilities	3,069,285	3,377,550
Nonfederal generation:		
Columbia Generating Station	2,487,355	2,327,455
Cowlitz Falls	116,780	122,410
Nonfederal generation	2,604,135	2,449,865
Lease financing program	559,556	449,695
Sponsored conservation:		
Conservation and Renewable Energy System	11,200	13,685
Tacoma	6,675	8,180
Sponsored conservation	17,875	21,865
Northern Wasco	21,740	22,785
Total	\$ 6,272,591	\$ 6,321,760

Prior to commercial operations, BPA acquired 100 percent and 70 percent of the generating capability of Energy Northwest's Nuclear Project No. 1 and Nuclear Project No. 3, respectively. The contracts require BPA to cover the costs of all maintenance expense and debt service on debt issued by nonfederal entities. Nuclear Project No. 1 and Nuclear Project No. 3 were terminated prior to completion.

BPA acquired all of the generating capability and agreed to pay the operating, maintenance and debt service costs of Energy Northwest's CGS nuclear generating project and of Lewis County PUD's Cowlitz Falls Hydroelectric Project.

Related assets for operating projects are included in nonfederal generation. Nonoperating projects are included in regulatory assets.

The underlying debt for the Energy Northwest obligations (comprising terminated nuclear facilities and CGS) matures through 2024 with interest rates that are fixed between 2.5 percent and 7.1 percent. Energy Northwest debt of \$1.37 billion is callable, in whole or in part, at Energy Northwest's option, on call dates between July 2013 and July 2021 at 100 percent of the principal amount.

The fair value of Energy Northwest debt exceeded recorded value by \$672.7 million and \$714.6 million as of Sept. 30, 2011, and 2010, respectively. The valuations are based on a market input evaluation pricing methodology using a combination of market observable data such as current market trade data, reported bid/ask spreads and institutional bid information. The weighted-average interest rate was 5.1 percent and 5.2 percent for the Energy Northwest CGS, Nuclear Project No. 1, and Nuclear Project No. 3 portion of outstanding nonfederal debt as of Sept. 30, 2011, and 2010, respectively.

Under the Lease Financing Program, BPA consolidates five special purpose corporations, collectively referred to as Northwest Infrastructure Financing Corporations (NIFCs), which issue debt to and receive advances from nonfederal sources. The combined NIFCs have issued \$119.6 million in bonds and borrowed \$440.0 million on lines of credit with various banks. The bonds bear interest at 5.4 percent per annum and mature in 2034. All NIFC bonds outstanding are subject to redemption by NIFC, in whole or in part, at any date, at the higher of the principal amount of the bonds or the present value of the bonds discounted using the U.S. Treasury rate plus a premium of 12.5 basis points. The lines of credit become due in full at various dates ranging between July 1, 2014, and July 1, 2016. On the accompanying Combined Balance Sheets, the bonds and bank credit facilities are included in Nonfederal debt and the leased assets are primarily included in Utility plant and also in Deferred charges and other for unspent funds.

The fair value of the combined NIFC bonds and lines of credit exceeded the recorded value by \$45.0 million and \$33.3 million as of Sept. 30, 2011, and Sept. 30, 2010, respectively. The valuations are based on the discounted future cash flows using interest rates for similar debt which could have been issued at Sept. 30, 2011, and 2010, respectively. The weighted-average interest rate on the NIFCs' outstanding debt was 4.0 percent and 4.6 percent as of Sept. 30, 2011, and Sept. 30, 2010, respectively.

BPA has agreed to fund debt service on Conservation and Renewable Energy System and City of Tacoma Conservation bonds issued to finance conservation programs sponsored by BPA.

The Northern Wasco Hydro Project agreement was terminated by the Settlement and Termination Agreement between BPA and the Northern Wasco PUD on April 25, 1995. The Settlement Agreement requires BPA to pay the trustee annual debt service as required by the Bond Resolution.

Nonfederal debt includes both operating and nonoperating projects. BPA recognizes expenses for these projects based upon total project cash funding requirements, which include debt service and operating and maintenance expenses. BPA recognized operating and maintenance expense for these projects of \$328.1 million, \$262.6 million and \$291.0 million in fiscal years 2011, 2010 and 2009, respectively, which is included in Operations and maintenance in the accompanying Combined Statements of Revenues and Expenses. Debt service for the projects of \$625.0 million, \$600.4 million and \$501.4 million for fiscal years 2011, 2010 and 2009, respectively, is reflected as Nonfederal projects in the accompanying Combined Statements of Revenues and Expenses.

MATURING NONFEDERAL DEBT

As of Sept. 30 — thousands of dollars

2012	\$	429,545
2013		494,915
2014		714,842
2015		791,136
2016		841,187
2017 and thereafter		3,000,966
Total	\$	6,272,591

1989 Letter Agreement

In 1989, BPA 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.

VARIABLE INTEREST ENTITIES

Upon adoption of the update to consolidation accounting, BPA reviewed the arrangements with the five NIFC entities and determined that BPA continues to be the primary beneficiary of these VIEs. The key factor in this determination is BPA's ability to direct the commercial and operating activities of the transmission facilities underlying the lease agreements. Additionally, BPA's lease agreements with the NIFC entities obligate BPA to absorb the operational and commercial risks, and thus potentially significant benefits or losses, associated with the underlying transmission facilities.

Under the lease purchase agreements, the NIFCs issue debt to finance the construction of the transmission facilities which are then leased to BPA. The collateral for the debt is the lease payment stream from BPA. The NIFC entities hold legal title to the transmission facilities during the lease term and BPA serves as the construction agent for these leased assets. BPA also has exclusive use and control of the assets during the lease periods and has indemnified the equity owners of the NIFCs for all construction and operating risks associated with the leased transmission facilities. At the end of each lease term, BPA has the option to buy the transmission facilities at a bargain purchase price. BPA provides certain administrative services as construction agent to the NIFCs and is obligated to indemnify certain expenses of the NIFCs related to their respective projects.

Amounts related to the NIFC entities included on the Combined Balance Sheets include Deferred charges and other of \$33.5 million and \$28.8 million and Nonfederal debt of \$559.6 million and \$449.7 million as of Sept. 30, 2011, and 2010, respectively.

9. Residential Exchange Program

BACKGROUND

As provided in the Pacific Northwest Electric Power Planning and Conservation Act (Northwest Power Act), beginning in 1981 BPA entered into 20-year Residential Purchase and Sale Agreements (RPSAs) with eligible regional utility customers. The RPSAs implemented the REP.

In 2000, BPA signed Residential Exchange Program Settlement Agreements ("REP settlements" or "settlement agreements") with the region's six IOUs under which BPA provided monetary and power benefits as a

settlement of Residential Exchange disputes for the period July 1, 2001, through Sept. 30, 2011. BPA later signed additional agreements and amendments with IOU customers related to the settlement agreements. One such agreement provided for the elimination or deferral of certain IOU benefit payments, while later agreements and amendments provided for minimum and maximum amounts for the IOU monetary benefits for fiscal years 2007 through 2011, provided that BPA would have no obligation to provide power to the IOUs in this period. When future amounts were committed through these agreements, BPA recorded a REP settlement liability for the minimum committed amounts and a regulatory asset for amounts recoverable in future rates.

LOOKBACK AMOUNT

In May 2007, the Ninth Circuit Court ruled that the REP settlements were inconsistent with the Northwest Power Act and that BPA improperly allocated settlement costs to BPA's preference rates. In response to that ruling, in fiscal year 2008 BPA reduced the REP settlement agreement liability and regulatory asset to zero and conducted the 2007 Supplemental Wholesale Power Rate Case (WP-07 Supplemental Rate Case).

On Sept. 22, 2008, the BPA administrator issued a Final Record of Decision (ROD) that revised power rates for fiscal year 2009 and determined the amount the COUs were overcharged in prior years. A portion of the prior overcharges, which amounted to \$746.2 million for fiscal years 2002 through 2006, were labeled the "Lookback Amount" in the Final ROD. This Lookback Amount represented amounts over-collected from COUs in prior years' rates, which also represented the amounts overpaid to the IOUs under the settlement agreements in prior years. As described in the WP-07 Supplemental Rate Case and in the 2010 Wholesale Power and Transmission Rate Adjustment Proceeding (WP-10 Rate Case), the BPA administrator designated the amount to be recovered from each IOU and returned to the qualifying COUs. These amounts did not reduce rates, but were applied as credits to qualifying COUs as designated in the corresponding Final RODs. BPA recognized the refund and reduced expense in the year it was applied. These transactions were net revenue neutral as the same amount reduced both revenue and expense. The Lookback Amount was recorded as both a regulatory asset, representing amounts to be collected from IOUs through future rate proceedings, and a regulatory liability, representing amounts to be credited to the COUs in future rates.

After recording the Lookback Amount for fiscal year 2010 of \$82.1 million, the Lookback Amount ending balance including interest as of Sept. 30, 2010, was \$568.5 million. In 2011, BPA adjusted both the regulatory liability and regulatory asset to \$565.4 million to reflect the changes resulting from the 2012 Settlement Agreement.

IOU EXCHANGE BENEFITS

In fiscal year 2008, Interim Agreements were executed to provide certain IOUs with temporary REP benefits for their residential and small farm consumers. These agreements included a provision to true up the amounts advanced with the actual REP benefits for fiscal year 2008. The true up amount for the IOUs was \$69.6 million; however, provisions in the agreement provided that true up payments could not be paid until any subsequent legal challenges to BPA's final ROD, if any, are resolved. (See Note 13, Commitments and Contingencies.) As yet, all legal challenges related to this program have not been resolved.

In 2009, BPA reached a settlement with Avista over its disputed deemer balance, which resulted in the amount due to it for its 2008 benefits changing from zero to \$12.0 million and an increase in the IOU exchange benefits balance to \$81.6 million. After applying interest for fiscal year 2011, this balance has increased to \$86.4 million.

2009 DEEMER ADJUSTMENT

As noted above, in June 2009, BPA reached a settlement regarding a long standing dispute with Avista Corporation over the REP deemer account provisions. Deemer balances result when a REP exchanging utility's average system cost is below the BPA priority firm exchange rate. Rather than resulting in a requirement of the exchanging utility to pay BPA for the exchange, the utility deems its average system cost to be equal to the priority firm exchange rate. The amount that otherwise would have been owed to BPA is accumulated and offset against future benefits until the deemer account is reduced to zero. Upon elimination of the deemer account balance, the exchanging utility is entitled to receive payment for exchange benefits. The

settlement with Avista set the beginning fiscal year 2002 deemer balance to \$55.0 million, rather than the disputed deemer account balance of \$85.6 million.

The accumulated effect of the Avista settlement resulted in higher REP expense recorded in fiscal year 2009 of \$20.5 million and lower revenues due to the effect of the Avista Lookback Amount applied of \$12.5 million that was recorded as revenue subject to refund. The total effect was a reduction to Net revenue of \$33.0 million for fiscal year 2009.

2012 RESIDENTIAL EXCHANGE PROGRAM SETTLEMENT AGREEMENT

Beginning in April 2010, over 50 litigants and other regional parties entered into mediation to resolve their numerous disputes over the REP. Participants reached an agreement in principle in early September 2010 and in February 2011 reached a final settlement agreement – the 2012 Residential Exchange Program Settlement Agreement (Settlement Agreement). In March 2011, BPA distributed the Settlement Agreement for regional entities' consideration and signature. In conjunction with the customers' settlement agreement efforts, in December 2010 BPA initiated the Residential Exchange Program Settlement Agreement Proceeding (REP-12) to evaluate the Settlement Agreement and determine whether it was in the region's best interest for the administrator to sign the Settlement Agreement on behalf of BPA. In July 2011, the administrator signed the REP-12 Final ROD and the Settlement Agreement.

In 2011, BPA recorded a long-term liability and corresponding regulatory asset of \$3.07 billion associated with the Settlement Agreement. Beginning in fiscal year 2012, under the provisions of the Settlement Agreement the IOUs receive Scheduled Amounts starting at \$182.1 million with increases over time to \$286.1 million as the final payment in fiscal year 2028. The distribution of these payments will depend on each IOUs' average system cost and exchange load, plus adjustments to reflect Lookback Amounts recovered from IOUs in fiscal years 2009 through 2011. The settled Scheduled Amounts to be paid to the IOUs total \$4.07 billion over the 17-year period. Amounts recorded of \$3.07 billion represent the present value of future cash outflows for these exchange benefits.

In addition to Scheduled Amounts, the Settlement Agreement calls for Refund Amounts to be paid of \$76.5 million each year beginning in fiscal year 2012 through fiscal year 2019. The Refund Amounts replace the Lookback Amounts and are accounted for similar to the Lookback Amounts in that a regulatory asset and liability have been established for the refunds that will be provided to BPA customers as credits on customer monthly bills. The Settlement Agreement replaces the Lookback Amounts that were reduced to zero as of Sept. 30, 2011, with the Refund Amounts totaling \$612.3 million. Amounts recorded of \$565.4 million represent the present value of future cash flows for the amounts to be refunded to customers, as well as reduced exchange benefits. The distribution of the Refund Amount will be split between customers with 50 percent of the Refund Amounts (\$38.3 million per year) returned to COUs based on the percentages BPA established in the WP-10 rate proceeding. The remaining 50 percent will be returned to COUs based on each customer's expected share of Tier 1 load as defined in BPA's 2012 Wholesale Power and Transmission Rate Adjustment Proceeding.

10. Deferred Credits and Other

<i>As of Sept. 30 — thousands of dollars</i>	2011	2010
Generation interconnection agreements	\$ 279,048	\$ 251,206
Customer reimbursable projects	238,317	233,045
Third AC Intertie capacity agreements	101,221	103,904
Capital leases	35,619	36,652
Fiber optic leasing fees	32,722	35,371
Federal Employees' Compensation Act	31,352	29,945
Settlements	28,500	28,500
Derivative instruments	27,422	51,563
Other	7,906	13,272
Total	\$ 782,107	\$ 783,458

Deferred credits and other include the following items:

“Generation interconnection agreements” are generators’ advances held as security for requested new network upgrades and interconnection. These advances accrue interest and will be returned as credits against future transmission service on the new or upgraded lines.

“Customer reimbursable projects” consist of advances received from customers where either the customer or BPA will own the resulting asset. 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, the revenue is recognized over the life of the asset once the corresponding asset is placed in service.

“Third AC Intertie capacity agreements” reflect unearned revenue from customers related to the Third AC Intertie capacity project. Revenue is being recognized over an estimated 49-year life of the related assets.

“Capital leases” represent BPA’s long-term portion of capital lease liabilities that are not part of the Lease Financing Program. (See Note 8, Nonfederal Financing.)

“Fiber optic leasing fees” reflect unearned revenue related to the leasing of the fiber optic cable. Revenue is being recognized over the lease terms extending out to 2020.

“Federal Employees’ Compensation Act” reflects the actuarial estimated amount of future payments for current recipients of BPA’s worker compensation benefits.

“Settlements” reflect amounts accrued to settle outstanding litigation. (See Note 13, Commitments and Contingencies.)

“Derivative instruments” reflect the unrealized fair value loss of the derivative portfolio which includes physical power purchase and sale transactions and a heat rate option contract.

11. Risk Management and Derivative Instruments

BPA is exposed to various forms of market risk including commodity price risk, commodity volumetric risk, interest rate risk, credit risk and event risk. Non-performance risk, which includes credit risk, is described in Note 12, Fair Value Measurements. BPA has formalized risk management processes in place to manage agency risks, including the use of derivative instruments. The following describes BPA’s exposure to and management of risks.

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 market risk and determines the transactional risk

policy and control environment at BPA. Through simulation and analysis of the hydro supply system, experienced business and risk managers install market price risk measures to capture additional market related risks, including credit and event risk.

COMMODITY PRICE RISK AND VOLUMETRIC RISK

Primarily due to the variation in the available energy from its hydroelectric generation capacity, BPA enters into short-term and long-term forward sales and purchase agreements in the wholesale markets to balance its energy supply and demand. Commodity price risk results from fluctuations in the electric market prices in the Pacific Northwest that affects the value of the energy inventory bought and sold, as well as the value of prior purchase and sale contracts. In fiscal year 2011, there was a net surplus and sale of energy above that needed to serve the region's firm load obligations.

BPA measures the market price risk in its portfolio on a daily, weekly and monthly basis employing both parametric calculations and non-parametric Monte Carlo simulations to derive net revenues at risk, mark-to-market, value at risk and additional risk metrics as appropriate. These methods provide 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 standard measures such as sensitivity and scenario testing to determine the impacts of a sudden change in market price, volatility, correlations or hydro inventory. These methods assume hypothetical movements in future market prices and in hydro inventory and provide an estimate of possible net revenues outcomes for BPA's portfolios. In response to market price risk, futures, forwards, swaps and option instruments may be used to mitigate BPA's exposure to price fluctuations.

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 deliver or take delivery of electricity. BPA's counterparties are generally large and stable and do not represent a significant concentration of credit risk. Credit risk is mitigated at BPA by reviewing counterparties for creditworthiness, establishing credit limits and monitoring credit exposure on a daily basis. To further manage credit risk, BPA obtains credit support such as letters of credit, parental guarantees, cash in the form of prepayment and/or deposit of escrow from some counterparties. Counterparties are monitored closely for changes in financial condition and credit reviews are updated regularly. 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.

During fiscal year 2011, BPA experienced no significant losses as a result of any customer defaults or bankruptcy filings. At Sept. 30, 2011, BPA had \$43.1 million in credit exposure to purchase and sale contracts taking into account netting rights. BPA's credit exposure, net of cash collateral, to sub-investment grade counterparties was less than one percent of total outstanding credit exposures. BPA's top five credit exposures were \$34.8 million, or 80.7 percent, of the total credit exposure. The majority of this exposure is mark-to-market exposure arising from a term transaction with an "AA-" rated municipality with ratemaking authority.

INTEREST RATE RISK

BPA has the ability to issue variable rate debt to the U.S. Treasury. As of Sept. 30, 2011, BPA had no outstanding variable rate U.S. Treasury debt. (See Note 7, Borrowings from U.S. Treasury.)

DERIVATIVE INSTRUMENTS

BPA follows the Derivatives and Hedging accounting guidance that requires every derivative instrument be recorded on the balance sheet as an asset or liability measured at its fair value and also requires that a change in the derivative's fair value be recognized currently in earnings unless specific hedge accounting criteria are met.

COMMODITY CONTRACTS

It is BPA's policy to document and apply as appropriate the normal purchases and normal sales exception allowed under Derivatives and Hedging accounting guidance. Forward electricity contracts are generally considered normal purchases and normal sales if they require physical delivery, are expected to be used or sold by BPA in the normal course of business and meet the definition of capacity described in the Derivatives and Hedging accounting guidance. These transactions are not required to be recorded at fair value in the financial statements. Recognition of these contracts in Sales or Purchased power in the Combined Statements of Revenues and Expenses occurs when the contracts settle.

In fiscal year 2010, BPA began applying Regulated Operations accounting treatment to its derivative instruments that are recorded at fair value and do not meet the normal purchases and normal sales exception. As a result, BPA recognized a loss of \$16.4 million in fiscal year 2010 which was primarily comprised of the net derivative balance for commodity contracts at the beginning of the year.

Prior to this adoption, BPA recorded the changes in fair value under Derivative instruments in the current period in the Combined Statements of Revenues and Expenses. When available, quoted market prices or prices obtained through external sources are used to measure a contract's fair value. For contracts without available quoted market prices, fair value is determined based on internally developed modeled prices. (See Note 12, Fair Value Measurements.)

At Sept. 30, 2011, the derivative commodity contracts recorded at fair value totaled 10.4 million MWh (gross basis). BPA records realized and unrealized gains and losses on commodity contract derivative transactions in the operating section as non-cash adjustments in the Combined Statements of Cash Flows. BPA does not apply hedge accounting.

INTEREST RATE SWAP TRANSACTIONS

In fiscal year 2010, BPA terminated two floating-to-fixed LIBOR interest rate swaps which had been used to help manage interest rate risk related to its long-term variable Energy Northwest debt portfolio. BPA terminated both swaps in conjunction with its debt management action to refinance the related variable rate debt into fixed rate debt. This resulted in the realization of a \$29.4 million loss, which was included in nonfederal projects expenses, and the corresponding removal of the \$31.2 million unrealized loss from Derivative instruments under Operating revenues.

DERIVATIVE ASSETS AND LIABILITIES MEASURED AT FAIR VALUE

<i>As of Sept. 30 — thousands of dollars</i>	2011	2010
Assets		
Derivative instruments ¹		
Commodity contracts, gross	\$ 47,140	\$ 22,829
Less: netting ²	(14,760)	(2,147)
Total, net	\$ 32,380	\$ 20,682
Liabilities		
Derivative instruments ¹		
Commodity contracts, gross	\$ (42,182)	\$ (53,710)
Less: netting ²	14,760	2,147
Total, net	\$ (27,422)	\$ (51,563)

¹ Derivative instruments assets and liabilities are included in Deferred charges and other and Deferred credits and other in the Combined Balance Sheets, respectively. (See Note 5, Deferred Charges and Other and Note 10, Deferred Credits and Other.)

² Netting represents a balance sheet adjustment for same counterparty master netting arrangements.

Derivative instruments unrealized gains of \$37.4 million and unrealized losses of \$33.9 million were recorded in regulatory assets and liabilities in the Combined Balance Sheets in fiscal years 2011 and 2010, respectively. The following table presents the effect of derivative instruments gains and losses on the Combined Statements of Revenues and Expenses.

AMOUNT OF GAIN (LOSS) RECOGNIZED

<i>As of Sept. 30 — thousands of dollars</i>		2011	2010	2009
	Location of Gain (Loss) Recognized in Net Revenues (Expenses)			
Commodity contracts	Derivative instruments	\$ —	\$ (16,446)	\$ (17,356)
Interest rate swaps	Derivative instruments	—	31,246	(18,680)
Subtotal		—	14,800	(36,036)
Interest rate swaps	Nonfederal projects	—	(29,422)	(7,450)
Total		\$ —	\$ (14,622)	\$ (43,486)

12. Fair Value Measurements

BPA applies the Fair Value Measurements and Disclosures accounting guidance for all financial instruments (recurring and nonrecurring) and for all nonfinancial instruments subject to recurring fair value measurement. This accounting guidance defines fair value, establishes a framework for measuring fair value in accordance with generally accepted accounting principles and prescribes disclosures about fair value measurements. BPA applied fair value measurements to certain assets and liabilities including commodity and interest rate derivative instruments and nuclear decommissioning trusts and other investments in accordance with the accounting guidance.

In accordance with the Fair Value Measurements and Disclosures accounting guidance, BPA maximizes the use of observable inputs and minimizes the use of unobservable inputs when measuring fair value. Fair value is based on actively quoted market prices, if available. In the absence of actively quoted market prices, BPA seeks price information from external sources, including broker quotes and industry publications. If pricing information

from external sources is not available, BPA uses forward price curves derived from internal models based on perceived pricing relationships to major trading hubs.

BPA also utilizes the following fair value hierarchy, which prioritizes the inputs to valuation techniques used to measure fair value, into three broad levels:

Level 1 – Quoted prices (unadjusted) in active markets for identical assets and liabilities that BPA has the ability to access at the measurement date. Instruments categorized in Level 1 primarily consist of financial instruments such as fixed income, equity mutual funds and money market funds.

Level 2 – Inputs other than quoted prices included within Level 1 that are either directly or indirectly observable for the asset or liability, including quoted prices for similar assets or liabilities in active markets, quoted prices for identical or similar assets or liabilities in inactive markets, inputs other than quoted prices that are observable for the asset or liability, and inputs that are derived from observable market data by correlation or other means. Instruments categorized in Level 2 include certain non-exchange traded derivatives and certain agency securities as part of the special purpose corporations' trust funds investments.

Level 3 – Unobservable inputs for the asset or liability, including situations where there is little, if any, market activity for the asset or liability. Instruments categorized in Level 3 include long dated and modeled commodity contracts.

The fair value hierarchy gives the highest priority to quoted prices in active markets (Level 1) and the lowest priority to unobservable data (Level 3). In some cases, the inputs used to measure fair value might fall in different levels of the fair value hierarchy. The lowest level input that is significant to a fair value measurement in its entirety determines the applicable level in the fair value hierarchy. Assessing the significance of a particular input to the fair value measurement in its entirety requires judgment, considering factors specific to the asset or liability.

In accordance with the Fair Value Measurements and Disclosures accounting guidance, BPA includes non-performance risk in calculating fair value measurements. This includes a credit risk adjustment based on the credit spreads of BPA's counterparties when in an unrealized gain position, or on BPA's own credit spread when in an unrealized loss position. BPA's assessment of non-performance risk is generally derived from the credit default swap market and from bond market credit spreads. The impact of the credit risk adjustments for all outstanding derivatives was immaterial to the fair value calculation at Sept. 30, 2011, and 2010.

ASSETS AND LIABILITIES MEASURED AT FAIR VALUE ON A RECURRING BASIS

As of Sept. 30, 2011 — thousands of dollars

	Level 1	Level 2	Level 3	Netting ²	Total
Assets					
Nonfederal nuclear decommissioning trusts					
U.S. government obligation mutual funds	\$ 86,834	\$ —	\$ —	\$ —	\$ 86,834
Equity index funds	74,923	—	—	—	74,923
Corporate bond index funds	37,028	—	—	—	37,028
Cash and cash equivalents	24	—	—	—	24
Derivative instruments ¹					
Commodity contracts	—	21,058	26,082	(14,760)	32,380
Special purpose corporations' trust funds					
U.S. government obligations	—	125,547	—	—	125,547
U.S. government sponsored enterprise obligations	—	1,052	—	—	1,052
Total	\$198,809	\$147,657	\$ 26,082	\$(14,760)	\$357,788
Liabilities					
Derivative instruments ¹					
Commodity contracts	\$ —	\$(40,743)	\$ (1,439)	\$ 14,760	\$(27,422)
Total	\$ —	\$(40,743)	\$ (1,439)	\$ 14,760	\$(27,422)

As of Sept. 30, 2010 — thousands of dollars

Assets					
Nonfederal nuclear decommissioning trusts					
U.S. government obligation mutual funds	\$105,999	\$ —	\$ —	\$ —	\$105,999
Equity index funds	80,867	—	—	—	80,867
Corporate bond index funds	1,954	—	—	—	1,954
Cash and cash equivalents	30	—	—	—	30
Derivative instruments ¹					
Commodity contracts	—	2,329	20,500	(2,147)	20,682
Special purpose corporations' trust funds					
U.S. government obligations	—	89,012	—	—	89,012
U.S. government sponsored enterprise obligations	—	6,898	—	—	6,898
Total	\$188,850	\$ 98,239	\$ 20,500	\$ (2,147)	\$305,442
Liabilities					
Derivative instruments ¹					
Commodity contracts	\$ —	\$(50,865)	\$ (2,845)	\$ 2,147	\$(51,563)
Total	\$ —	\$(50,865)	\$ (2,845)	\$ 2,147	\$(51,563)

¹ Derivative instruments assets and liabilities are included in Deferred charges and other and Deferred credits and other in the Combined Balance Sheets, respectively. (See Note 5, Deferred Charges and Other and Note 10, Deferred Credits and Other.) See Note 11, Risk Management and Derivative Instruments for more information related to BPA's risk strategy and use of derivative instruments.

² Netting represents a balance sheet adjustment for same counterparty master netting arrangements.

COMMODITY CONTRACTS

The following table presents the changes in the assets and liabilities measured at fair value on a recurring basis and included in the Level 3 fair value category.

<i>For the year ended Sept. 30 — thousands of dollars</i>	2011	2010
Beginning Balance	\$ 17,655	\$ 28,190
Total realized and unrealized gains (losses) included in:		
Net revenues (expenses) ¹	—	(25,209)
Regulatory assets and liabilities ²	6,988	14,674
Purchases, issuance and settlements	—	—
Transfers in (out) of Level 3	—	—
Ending Balance	\$ 24,643	\$ 17,655
The amount of total gains (losses) for the fiscal year included in		
Net revenues (expenses) attributable to the change in unrealized		
gains (losses) relating to contracts still held at the reporting date ¹	\$ —	\$ (23,837)

¹ Prior to BPA's application of Regulated Operations accounting treatment to its derivative instruments in fiscal year 2010, unrealized gains and losses were included in Derivative instruments in the Combined Statements of Revenues and Expenses.

² Subsequent to BPA's application of Regulated Operations accounting treatment to its derivative instruments in fiscal year 2010, unrealized gains and losses are included in Regulatory assets and liabilities in the Combined Balance Sheets.

13. Commitments and Contingencies

INTEGRATED FISH AND WILDLIFE PROGRAM

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 projects that are consistent with the Northwest Power Act and that are consistent with the Pacific Northwest Power and Conservation Council's Columbia River Basin Fish and Wildlife Program. In addition, certain fish species are listed 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 (BiOp) prepared by the National Oceanic and Atmospheric Administration Fisheries Service and the U.S. Fish and Wildlife Service in furtherance of the ESA. BPA's total commitment including timing of payments under the Northwest Power Act, ESA and BiOp is not fixed or determinable. However, the current estimate of long-term fish and wildlife agreements with a contractual commitment which BPA has entered into is \$1.03 billion. These agreements will expire at various dates between fiscal years 2018 and 2025.

IRRIGATION ASSISTANCE

Scheduled distributions

As of Sept. 30 — thousands of dollars

2012	\$	1,182
2013		58,823
2014		52,427
2015		51,989
2016		60,814
2017 and thereafter		440,855
Total	\$	666,090

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. In establishing power rates, particular statutory provisions guide the assumptions that BPA makes as to the amount and timing of such distributions. 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. Future irrigation assistance payments are scheduled to total \$666.1 million over a maximum of 66 years since the time the irrigation facilities were completed and placed in service. BPA is required by the Grand Coulee Dam - Third Powerplant Act to demonstrate that reimbursable costs of the FCRPS will be returned to the U.S. Treasury from BPA within the period prescribed by law. BPA is required to make a similar demonstration for the costs of irrigation projects to the extent the costs have been determined to be beyond the irrigators' ability 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. Irrigation assistance excludes \$40.3 million for Teton Dam which failed prior to completion and for which BPA has no obligation to recover these costs.

FIRM PURCHASE POWER COMMITMENTS

As of Sept. 30 — thousands of dollars

2012	\$	51,805
2013		66,441
2014		35,234
Total	\$	153,480

When BPA forecasts a resource shortage based on expected obligations and the historical water record for the Columbia River basin, BPA takes a variety of steps to cover the shortage. If appropriate, BPA will enter into long-term commitments to purchase power for future delivery. The above table includes firm purchase power agreements of known cost that are currently in place to assist in meeting expected future obligations under long-term power sales contracts. Included are six contracts for winter purchases through fiscal year 2014 and three purchases made specifically to meet BPA's commitments to sell power at Tier 2 rates in fiscal years 2012 and 2013. The expense associated with the winter purchases for 2011 and 2010 were \$43.4 million and \$43.1 million, respectively. Delivery for Tier 2 purchases does not commence until fiscal year 2012. There were no purchases made under any of the contracts prior to 2010. BPA has several power purchase agreements

with wind powered and other generating facilities that are not included in the table above as payments are based on the variable amount of future energy generated and there are no minimum payments required.

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 insurance policies purchased from NEIL by BPA include: 1) Primary Property and Decontamination Liability Insurance; 2) Decontamination Liability, Decommissioning Liability and Excess Property Insurance; and 3) NEIL I Accidental Outage Insurance.

Under each insurance policy, BPA could be subject to a retrospective premium 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 Liability Insurance policy is \$9.1 million. For the Decontamination Liability, Decommissioning Liability and Excess Property Insurance policy, the maximum assessment is \$18.7 million. For the NEIL I Accidental Outage Insurance policy, the maximum assessment is \$5.0 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 \$375.0 million, BPA could be subject to a retrospective assessment of up to \$111.9 million limited to an annual maximum of \$17.5 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 may be identified as potential responsible parties. Costs associated with cleanup of sites are not expected to be material to the FCRPS' financial statements. As such, no material liability has been recorded.

LITIGATION

Southern California Edison

Southern California Edison (SCE) filed two separate actions pending in the U.S. Court of Federal Claims against BPA related to a power sales and exchange agreement (Sale and Exchange Agreement) between BPA and SCE. The actions challenged: 1) BPA's decision to convert the contract from a sale of power to an exchange of power as provided for under the terms of the contract (Conversion Claim); and 2) BPA's termination of the Sales and Exchange Agreement due to SCE's nonperformance (Termination Claim).

In 2006, BPA and SCE executed an agreement to settle the claims wherein BPA would make a payment of \$28.5 million plus applicable interest to SCE if certain identified conditions were met, including a final resolution of BPA's claims pending in the California refund proceedings and related litigation. BPA has recorded a liability in this amount on the basis that all conditions have been met except the final resolution in the California refund proceedings which management considers probable. BPA established an offsetting regulatory asset, as the costs will be collected in future rates.

California parties' refund claims

BPA was a party to proceedings at FERC that sought refunds for sales into markets operated by the California Independent System Operator (ISO) and the California Power Exchange (PX) during the California energy crisis of 2000-2001. BPA, along with a number of other governmental utilities, challenged FERC's refund authority over governmental utilities. In *BPA v. FERC*, 422 F.3d 908 (9th Cir. 2005) the Court found that governmental utilities, like BPA, were not subject to FERC's statutory refund authority. As a consequence of the Court's decision, three California investor-owned utilities along with the State of California filed breach of contract claims in the United States Court of Federal Claims against BPA. The complaints, filed in March 2007, alleged that BPA was contractually obligated to pay refunds on transactions where BPA received amounts in excess of mitigated market clearing prices established by FERC. The plaintiffs' contractual breach is premised upon a FERC finding that it retroactively reset the prices under the ISO and PX tariffs when it established these mitigated market clearing prices. BPA has separately appealed to the Ninth Circuit Court the FERC finding that it

retroactively reset the tariff prices. The plaintiffs' claims for relief exceed \$300 million. A trial on the liability portion of plaintiffs' contractual breach claim commenced in July 2010 and concluded in August 2010. Post trial briefs were filed during fall 2010 and closing arguments were held in February 2011, and BPA is awaiting the Court's ruling. The damages phase of the case will be tried only after the Court of Federal Claims rules on the liability portion. No date has been scheduled for the damages phase.

Rates

BPA's rates are frequently the subject of litigation. Most of the litigation involves claims that BPA's rates are inconsistent with statutory directives, are not supported by substantial evidence in the record, or are arbitrary and capricious. It is the opinion of BPA's general counsel that if any rate were to be rejected, the sole remedy accorded would be a remand to BPA to establish a new rate. BPA's flexibility in establishing rates could be restricted by the rejection of a BPA rate, depending on the grounds for the rejection. BPA is unable to predict, however, what new rate it would establish if a rate were rejected. If BPA were to establish a rate that was lower than the rejected rate, a petitioner may be entitled to a refund in the amount overpaid; however, BPA is required by law to set rates to meet all of its costs. Thus, it is the opinion of BPA's general counsel that BPA may be required to increase its rates to seek to recover the amount of any such refunds, if needed.

Currently pending before the Ninth Circuit Court are numerous challenges to the decisions BPA reached in the WP-07 Supplemental Rate Case and that were also incorporated in the WP-10 Rate Case. The petitioners in these cases challenge, among other issues, BPA's calculation of certain refunds (referred to as "Lookback Amounts") associated with rates charged to BPA's preference customers from fiscal years 2002 through 2008. These refunds resulted from BPA's implementation of an REP settlement in fiscal years 2002 through 2008 that was later found unlawful and payment of REP benefits to BPA's investor-owned utility customers under that settlement. Following extensive negotiations, representatives from most of the region's consumer- and investor-owned utilities reached a proposed agreement on how BPA should establish REP benefits and recover the costs of those benefits through rates for the fiscal year period 2002 through 2028. BPA conducted a formal evidentiary hearing to review the proposed settlement agreement, which was signed by the administrator on July 26, 2011. Since the 2012 REP Settlement Agreement completely replaces BPA's REP-related WP-07 Supplemental Rate Case and WP-10 Rate Case decisions, BPA and many consumer-owned utilities have filed a motion in Ninth Circuit Court to dismiss pending litigation challenging those decisions. Any changes in REP benefits or costs will be resolved through future rates. BPA has recorded regulatory assets, a liability and a regulatory liability for the effects of the Settlement Agreement. (See Note 9, Residential Exchange Program.)

Other

The FCRPS may be affected by various other legal claims, actions and complaints, including litigation under the Endangered Species Act, which may include BPA as a named party. Certain of these cases may involve material amounts. BPA is unable to predict whether the FCRPS will avoid adverse outcomes in these legal proceedings; however, BPA believes that disposition of pending matters will not have a materially adverse effect on the FCRPS' financial position or results of operations for fiscal year 2011.

Judgments and settlements are included in BPA's costs and recovered through rates. Except with respect to the SCE and REP matters described above, BPA management has not recorded a liability for the above legal matters.



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