

May 13, 2002

# Bonneville Power Administration

## Power Business Line

### Generation Accumulated Net Revenues for Financial-Based Cost Recovery Adjustment Clause (FB CRAC)

FY 2002 Second Quarter Review Forecast

\$ in Millions

	FY 2002 Forecasted Second Quarter Results
FY 2000 FB CRAC Audited Net Revenues	\$170
FY 2001 FB CRAC Audited Net Revenues	(\$418)
FY 2002 Unaudited Second Quarter Forecasted Net Revenues	\$70
<i>Energy Northwest Debt Service Adjustment for FY 2002</i>	(\$375)
<i>FAS 133 Adjustment</i>	(\$1)
<b>FY 2002 Unaudited Second Quarter Forecasted Accumulated Net Revenues</b>	<b>(\$554)</b>
<b>FB CRAC FY 2002 Trigger Point</b>	<b>(\$408)</b>

*FY 2001 August ANR Trigger Point was (\$386 M).*

*FY 2003 August ANR Trigger Point is (\$265 M)*

#### 1. What is driving the forecast of the FB CRAC to trigger this year?

Many complex factors contribute to our current forecast. The biggest is our worsening financial situation due to a significant drop in net revenues this year. This is largely a result of lower-than-average seasonal surplus hydropower, combined with unexpectedly low market prices for this power. Seasonal surplus power is power that is available when water conditions exceed the worst on record. Because we cannot count on this power, we do not use it to serve our firm loads. Instead, we sell it as seasonal surplus when it is available and as water conditions warrant. However, when setting rates, we assumed we would generate revenues from these surplus sales. In normal water years and under normal market conditions, BPA earns significant revenues from sales of this surplus. These revenues help keep our firm power rates down. But, unfortunately, this year we are not realizing the significant revenues from seasonal surplus that we forecast under average water conditions last June when we set rates.

#### 2. What are the uncertainties still inherent in the end of year forecast?

In the second quarter review forecast for the end-of-year net revenues, PBL must make certain assumptions of what the spring and summer will look like in terms of load, water availability, and market prices. There is still a lot of volatility that can occur between now and the end of August, when the determination will be made on whether the FB CRAC has triggered. Some of the key drivers are market prices, hydro conditions, LB CRAC and Slice true-ups, and actual expense levels. Any variation of these can change the net revenue situation.

The primary factors influencing our rate levels are:

- **Power Market Prices** – since we are net sellers of energy this year, the market price we receive for this power determines how much we receive from secondary sales. An increase in market prices will result in an increase in revenues.
- **Power Augmentation Costs** – an important uncertainty BPA faces is the amount of load we will be obligated to serve and the timing of Northwest aluminum plants returning to production. We also have some load buydown agreements expiring soon. As market prices have dropped, the costs of replacing these agreements with market purchases have dropped somewhat as well. If market prices increase, the cost of serving the additional load will go up as well.
- **Hydro Conditions** – the impacts of last year’s drought lingered in the form of low steam flows and last fall’s low reservoirs. In addition, the January-to-July runoff forecast is running a bit below normal. Together the effect has been to reduce hydropower output by about 450 average megawatts in the current year. If this holds up, energy production from the hydro system this year would be further reduced from the average conditions assumed when we set rates.
- **Overall Program Costs** – these do not include the cost of power augmentation, costs related to providing other subscription benefits, or fixed costs. While some cost categories are over the targets and others are under, on the whole we are on schedule to meet the program cost targets for this year. This year’s financial difficulties are not due to cost increases from the 1998 Cost Review recommendation.

### **3. What is the Power Business Line doing to manage costs for FY 2002?**

The Power Business Line has a current action plan in place to aggressively manage costs in FY 2002. Excluding the costs of Augmentation purchases, we have brought expense budgets for 2002 down to the aggressive targets in the rate case, which are based on the 1998 Cost Review, through net reductions of \$102 million relative to the start-of-year estimates. This is progress, but is not enough. We are continuing to work to bring down FY 2002 and out-year costs. The details for this plan are included in the letter to the region from Paul Norman dated May 2, 2002.

[http://www.bpa.gov/power/psp/rates/05-02-2002\\_Letter.pdf](http://www.bpa.gov/power/psp/rates/05-02-2002_Letter.pdf)

### **4. What is the impact of refinancing Energy Northwest (ENW) debt and Financial Accounting Standards (FAS) 133?**

When the FB CRAC design was developed, the effects of refinancing Energy Northwest debt and FAS 133 were considered. When ENW debt is refinanced, the proceeds are used to pay off federal debt early, thus having no impact on cash. Because of the way federal and non-federal debt are displayed on the Income Statement, the FB CRAC equation has to keep the debt neutral by keeping the same ENW debt service amount in the calculation that was in the rate case. This way, any time BPA refinances the ENW debt, it will not be reflected in the FB CRAC calculation.

Mark-to-market adjustments required by FAS 133 is not in the FB CRAC calculation either. The FAS 133 is not associated with any earned revenues or expenses, but instead a reporting function required by FERC on certain derivative instruments and hedging activities. Because it does not have any revenues or expenses associated with it, it is taken out of the FB CRAC calculation.

**5. How will customers be kept informed of BPA's Accumulated Net Revenues during the year?**

- Each quarter, BPA will post on its Web site preliminary, unaudited, year-to-date aggregate financial results for generation, including ANR.
- By January of each year, BPA will post on its Web site the audited AANR attributable to the generation function for the prior fiscal year ending September 30.
- In May and August of each year, at the same time that BPA posts its quarterly results, BPA will post on its Web site an end-of-year forecast of ANR attributable to the generation function.
- BPA will notify the customers by the end of August if the FB CRAC will trigger for the subsequent year.