
Management's Discussion and Analysis – 2nd Quarter

Net Revenues

Through the six months ended March 31, 2002, BPA incurred net expenses of \$63 million, compared with \$235 million net expenses for the same period a year ago. The \$172 million change is primarily the result of adoption during fiscal year 2001 of a new industry accounting standard, "Accounting for Derivative Instruments and Hedging Activities" (SFAS 133). The changes as a result of SFAS 133 reflect an accounting only adjustment with no corresponding cash impact. Excluding the SFAS 133 adjustments net expenses for the six months ended March 31, 2002, were \$65 million, compared with \$119 million net expenses for the same period ended in 2001. This improvement is due primarily to lower operating expenses. Other than SFAS 133 effects, both BPA operating revenues and purchased power expense have reduced commensurate with lower purchase and sales prices on the West coast and transmission revenues which increased in 2001 due to constraints on the California system.

Operating Revenues

Revenues from the sales of electricity and transmission of \$1.727 billion were down \$259 million or 13 percent compared to the same period of fiscal 2001. Revenues were down even though BPA increased power and transmission rates on Oct. 1, 2001. Revenues did not increase as much as projected in the rate case because market prices for discretionary power sales decreased to an average of 34 mills from the previous year average of 86 mills. For transmission products, projected sales in the short-term market did not materialize.

Mark-to-market gains on derivative instruments were \$1 million through March 31, compared to \$116 million loss recorded the first half of fiscal 2001. BPA expects the volatility associated with SFAS 133 to be reduced during fiscal year 2002 and beyond because of the change in treatment of "bookout" transactions under the standard.

Miscellaneous revenues decreased \$17 million. Other Transmission Business Line revenues and the U.S. Treasury credit for Colville decreased.

U.S. Treasury credits for fish decreased \$66 million as spot market prices for power decreased.

Operating Expenses

Operations and maintenance cost through the second quarter of fiscal 2002 increased \$80 million from the previous year. Conservation and renewables discount, fish & wildlife, marketing, and payments to the U.S. Treasury for underfunded Civil Service Retirement System costs increased at BPA.

BPA's expense for purchased power decreased \$395 million or 35 percent when compared to the period a year ago. The decreased expense was the result of a 5.5 million, approximately 56 percent, reduction of megawatt-hours purchased combined with lower market prices from the second quarter in fiscal 2001. Federal generation decreased by 1.9 million megawatt-hours or 5 percent from the same period in the prior year due to reduced firm loads.

Nonfederal projects debt service expense decreased \$152 million or 47 percent. Refinancing Energy Northwest bonds deferred some principal payments due in July of fiscal 2001 and 2002 into the future.

Settlement agreements with BPA's investor owned utility (IOU) customers for settlement of the period running from July 1, 2001 through Sept. 30, 2011, resulted in residential exchange expense increasing \$47 million or 200 percent. The agreements provide for both sales of power and cash payments to the IOUs.

In total, operating expenses decreased \$418 million, or 20 percent.

Interest Expense

Net interest expense increased \$23 million, or 14 percent, compared to the same period in 2001. Appropriated debt increased in fiscal 2001 with the revised cost allocation to power at Grand Coulee dam. Interest income earned on BPA's cash account with the U.S. Treasury is netted against interest expense. As BPA's cash balance has decreased over the past year, interest income has decreased and is reflected in the increased net interest expense.

Utility Plant

As the investment in utility plant increased so increased the construction work in progress by \$294 million or 42 percent over the balance at March 31, 2001.

Forecast Financial Condition

The current forecast for fiscal 2002 year-end financial reserves – cash and deferred borrowing authority – is that year-end reserves will be \$150 to \$350 million, compared to \$625 million, at Sept. 30, 2001.

Federal Columbia River Power System

Comparative Balance Sheets (Unaudited)

(Thousands of Dollars)

| | March 31 | |
|---|---------------------|---------------------|
| | 2002 | 2001 |
| Assets | | |
| Utility Plant | | |
| Completed plant | \$11,323,659 | \$11,120,899 |
| Accumulated depreciation | (3,940,073) | (3,713,204) |
| | 7,383,586 | 7,407,695 |
| Construction work in progress | 996,716 | 703,200 |
| Net utility plant | 8,380,302 | 8,110,895 |
| Nonfederal Projects | 6,176,059 | 6,399,694 |
| Trojan Decommissioning Cost | 66,710 | 73,414 |
| Conservation, net of accumulated amortization | 413,710 | 474,888 |
| Fish & Wildlife, net of accumulated amortization | 141,426 | 140,076 |
| Current Assets | 1,307,215 | 1,461,249 |
| Other Assets | 201,819 | 426,364 |
| | \$16,687,241 | \$17,086,580 |
| Capitalization and Liabilities | | |
| Accumulated Net Expenses | (\$284,626) | (\$101,928) |
| Federal Appropriations | 4,671,085 | 4,549,419 |
| Capitalization Adjustment | 2,226,078 | 2,294,148 |
| Long-Term Debt | 2,622,542 | 2,648,200 |
| Nonfederal Projects Debt | 5,958,230 | 6,043,650 |
| Trojan Decommissioning Reserve | 54,710 | 60,814 |
| Current Liabilities | 869,715 | 979,544 |
| Deferred Credits | 569,507 | 612,733 |
| | \$16,687,241 | \$17,086,580 |

The irrigation assistance distribution of \$16,560 for fiscal 2001 is included in accumulated net expenses.

Comparative Statements of Revenues and Expenses (Unaudited)

(Thousands of Dollars)

| | Six months ended | | Twelve months ended | |
|---|-------------------|--------------------|---------------------|--------------------|
| | March 31 | | March 31 | |
| | 2002 | 2001 | 2002 | 2001 |
| Operating Revenues: | | | | |
| Revenues | \$1,726,629 | \$1,985,344 | \$3,304,467 | \$3,620,075 |
| SFAS 133 mark-to-market gain (loss) | 1,319 | 52,315 | (3,119) | 52,315 |
| Other revenues | 17,191 | 33,746 | 50,347 | 55,508 |
| U.S. Treasury credits for fish | 26,158 | 92,217 | 534,649 | 0 |
| Operating Revenues | 1,771,297 | 2,163,622 | 3,886,344 | 3,727,898 |
| Operating Expenses: | | | | |
| Operations and maintenance | 506,158 | 426,380 | 1,034,876 | 930,415 |
| Purchased power | 738,704 | 1,133,720 | 1,896,945 | 1,699,309 |
| Tenaska | 0 | 0 | 0 | (26,817) |
| Non-Federal projects | 170,762 | 322,354 | 325,623 | 564,757 |
| Residential exchange | 70,910 | 23,647 | 115,345 | 55,570 |
| Federal projects depreciation | 160,923 | 159,468 | 324,769 | 326,171 |
| Operating Expenses | 1,647,457 | 2,065,569 | 3,697,558 | 3,549,405 |
| Net operating revenues | 123,840 | 98,053 | 188,786 | 178,493 |
| Interest Expense | 187,315 | 164,300 | 354,924 | 328,569 |
| Net expenses before cumulative effect of SFAS 133 | (63,475) | (66,247) | (166,138) | (150,076) |
| Cumulative Effect of SFAS 133 | 0 | (168,491) | 0 | (168,491) |
| Net Expenses | (\$63,475) | (\$234,738) | (\$166,138) | (\$318,567) |

Derivative Instruments and Hedging Activities

The SFAS 133 mark-to-market (MTM) amount is an "accounting only" (no cash impact) adjustment representing the MTM adjustment required by SFAS 133, as amended, for identified derivative instruments.

Operating Segments

The FCRP's major operating segments are defined by the utility functions of generation and transmission. The Power Business Line identifies the operations of the generation function, while the Transmission Business Line identifies the operations of the transmission function.

The business lines are not separate legal entities. Where applicable, "Corporate" represents items that are necessary to reconcile to the financial statements which generally include shared activity and eliminations. Each FCRPS segment operates predominantly in one industry and geographic region: the generation and transmission of electric power in the Pacific Northwest.

The FCRPS centrally manages all interest expense activity. Since the Bonneville Power Administration has one fund with the United States Department of Treasury, all cash and cash transactions are also centrally managed. Unaffiliated revenues represent sales to external customers for each segment. Intersegment revenues are eliminated as shown.

FCRPS management evaluates the performance of the business lines based on Net Operating Margin (NOM) and does not track the separate balance sheets or net revenues on a business line level. NOM represents revenues generated from operations less operating and maintenance expenses of the segment's revenue generating assets.

Major Customers

During fiscal 2002, and 2001, no single customer represented 10% or more of the FCRPS's revenues.

SFAS 131 SEGMENT REPORTING

(Thousands of Dollars)

| | Six months ended | | | |
|-----------------------------|---------------------|---------------------|--------------------|--------------------|
| | March 31 | | | |
| 2002 | | | | |
| | Power | Transmission | Corporate | Total |
| Unaffiliated Revenues | \$1,489,540 | \$281,757 | \$0 | \$1,771,297 |
| Intersegment Revenues | 38,671 | 59,083 | (97,754) | - |
| Operating Revenues | \$1,528,211 | \$340,840 | (97,754) | \$1,771,297 |
| Net Operating Margin | \$407,113 | \$180,030 | (\$88,185) | \$498,958 |
| 2001 | | | | |
| | Power | Transmission | Corporate | Total |
| Unaffiliated Revenues | \$1,952,987 | \$210,635 | \$0 | \$2,163,622 |
| Intersegment Revenues | 31,865 | 98,912 | (130,777) | - |
| Operating Revenues | \$1,984,852 | \$309,547 | (130,777) | \$2,163,622 |
| Net Operating Margin | \$337,972 | \$178,677 | (\$57,659) | \$458,990 |
| | | | | |
| | Twelve Months Ended | | | |
| | March 31 | | | |
| 2002 | | | | |
| | Power | Transmission | Corporate | Total |
| Unaffiliated Revenues | \$3,361,211 | \$525,133 | \$0 | \$3,886,344 |
| Intersegment Revenues | 70,200 | 152,833 | (223,033) | - |
| Operating Revenues | \$3,431,411 | \$677,966 | (223,033) | \$3,886,344 |
| Net Operating Margin | \$249,931 | \$365,175 | (\$192,113) | \$422,993 |
| 2001 | | | | |
| | Power | Transmission | Corporate | Total |
| Unaffiliated Revenues | \$3,316,736 | \$411,162 | \$0 | \$3,727,898 |
| Intersegment Revenues | 55,771 | 201,406 | (257,177) | - |
| Operating Revenues | \$3,372,507 | \$612,568 | (257,177) | \$3,727,898 |
| Net Operating Margin | \$741,024 | \$361,950 | (\$57,115) | \$1,045,859 |