ADMINISTRATOR'S RECORD OF DECISION

Sustainable Capital Financing Policy

July 2022

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1. INTRODUCTION

The Bonneville Power Administration (BPA) is a Federal power marketing administration that owns and operates more than 15,000 miles of high-voltage transmission lines and provides roughly 28 percent of the electric power used in the Pacific Northwest.[1] BPA is self-financing; it covers all of its costs by selling power and transmission services. Among other obligations, BPA is required by law to market Federal power and transmission and establish rates that recover its costs consistent with sound business principles. To that end, BPA has been granted a broad mandate to operate as a business and to take such actions as will ensure that BPA meets its various statutory obligations, including its debt repayment obligations to third parties and the U.S. Treasury.[2]

Meeting BPA's statutory duties requires a substantial amount of capital investment. The need for capital investments to replace and modernize aging Federal power and transmission infrastructure and support fish and wildlife restoration has grown to an unprecedented level. BPA's use of debt to finance this capital investment has a significant impact on its long-term financial strength and flexibility. As of the end of fiscal year (FY) 2021, BPA had $14.6 billion in outstanding debt.[3] This number is expected to grow by an additional $1.3 billion over the next six years. High debt levels increase BPA's future fixed costs through interest expense, which—all else equal—will increase future rates. Further, debt levels have a direct impact on debt-to-asset ratios. A high debt-to-asset ratio means higher fixed costs, which hampers BPA's financial flexibility. Limited flexibility in times of financial stress or volatility can result in an unstable cost of service over time. Furthermore, an entity's debt-to-asset ratio is a key financial indicator. A high ratio, while one of many factors considered, could negatively impact credit ratings for bonds supported by BPA's contractual commitments, which can result in higher interest rates. Sustainably managing BPA's debt-to-asset ratio is vital to ensuring the long-term financial health and viability of the Federal Columbia River Power System (FCRPS) for BPA's customers and their communities, and will help ensure a more consistent cost of service over time.

This Record of Decision (ROD) supports BPA's adoption of a new Sustainable Capital Financing Policy to guide its use of debt and revenue financing to finance its capital investments in a principled and predictable manner. Revenue financing refers to collecting cash through rates to finance a portion of the capital program rather than issue debt. Specifically, this policy establishes parameters to move away from predominantly 100 percent debt financing all capital investments, and toward revenue financing 10 percent of BPA's capital program as a baseline. The remaining 90 percent of the capital program would continue to be financed with debt. Additionally, the policy is designed to achieve a long-term business-line debt-to-asset ratio target. If a business unit is not forecast to achieve this target, additional revenue financing—constrained by rate impact—is added.

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[1] BPA Facts, https://www.bpa.gov/-/media/Aep/about/publications/general-documents/bpa-facts.pdf (2020).
[2] *See Ass'n of Pub. Agency Customers, Inc. v. Bonneville Power Admin.*, 126 F.3d 1158, 1171 (9th Cir. 1997).
[3] Bonneville Power Administration, *Annual Report 2021: Shaping the Future of Clean Energy* 55, *available at* https://www.bpa.gov/about/finance/-/media/aep/finance/annual-reports/ar2021.pdf ("BPA Annual Report 2021").

This policy is not purely mechanical, but allows flexibility to respond to changing circumstances.

2. BACKGROUND

2.1 BPA Manages Extensive Capital Assets in Support of Its Statutory Mission

Among other statutory obligations, BPA (along with the U.S. Army Corps of Engineers (Corps) and the U.S. Bureau of Reclamation (Reclamation)) is directed to operate and maintain the FCRPS.[4] With 31 dams, the FCRPS is the nation's largest hydroelectric producer of carbon-free electricity. Among the resources that produce power marketed by BPA is the output of the region's only commercial nuclear plant, the Columbia Generating Station.[5] BPA is also directed to maintain and operate the Federal Columbia River Transmission System, an interconnected system of high-voltage transmission lines that spans 15,000 circuit miles in six states. Together, BPA's power and transmission system produces more than $3 billion in annual sales.[6] The FCRPS power and transmission capital assets play a central role in the region's electrical system, and managing them in a cost-effective and economically efficient manner is a core part of BPA's statutory mission.

2.2 BPA Uses Various Tools to Finance and Manage Funding of Its Capital Investments

Supporting these assets requires significant capital investments. BPA's capital planning and decisions to invest in specific projects are separate and distinct decisions from BPA's decisions regarding the form of financing used to fund such projects. BPA has various tools at its disposal to finance and manage funding of its capital investments. These include appropriations, U.S. Treasury borrowing authority, capital leases, prepaid revenues, reserve financing, revenue financing, and early debt repayment. BPA also has the responsibility for the debt service on certain non-Federal projects. This debt service is incorporated in BPA's management of its entire debt portfolio. Financing decisions are not made at the individual project level. Rather, BPA takes a portfolio approach to the funding and other debt management associated with capital assets.

Appropriations

When BPA was first created, Congress appropriated funds to the Corps and Reclamation for construction of hydroelectric projects, for which BPA was (and remains) responsible for repaying the portion attributable to power purposes. For many years, BPA also received appropriations from Congress for construction of the transmission system. BPA's obligation begins when the capital investments are completed and placed in service, and

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[4] Federal Columbia River Transmission System Act, 16 U.S.C. § 838b (2018) ("Transmission System Act.").
[5] Bonneville Power Administration, BPA 2018-2023 Strategic Plan at 23 (Jan. 30, 2018), *available at* https://www.bpa.gov/-/media/Aep/projects/grid-modernization/2018-strategic-plan.pdf ("2018-2023 Strategic Plan").
[6] *Id.*

must be repaid in a period not to exceed 50 years for Power.[7] Unlike U.S. Treasury borrowing authority, appropriations are not revolving; they expire once repaid.

U.S. Treasury Borrowing Authority

By the early 1970s, Congress recognized that BPA would need a reliable source of capital funding apart from annual appropriations to facilitate long-term investment in transmission facilities.[8] In the Transmission System Act of 1974, Congress authorized BPA to issue bonds and other debt securities to the U.S. Treasury.[9] This authority is now referred to by BPA as Treasury borrowing authority. Unlike appropriations, the Treasury borrowing authority is like a revolving line of credit, meaning that BPA may borrow on the line of credit up to the statutory limit, with new borrowings depleting the amount available and repayment of prior borrowings replenishing the line of credit. Over time, Congress expanded the authorized uses for the Treasury borrowing authority and increased the amount available. Most recently, the Infrastructure Investment and Jobs Act increased the amount by $10 billion, bringing BPA's total Treasury borrowing authority cap to $17.7 billion.[10] Of the $17.7 billion, $13.7 billion is currently available, with the full $17.7 billion becoming available beginning in FY 2028. The proceeds of bonds issued to the Treasury are available to both Power and Transmission to finance capital investments needed to meet BPA's statutory obligations.[11]

Capital Leases

BPA may enter into lease agreements with third parties to finance investments over time.[12] BPA has used this authority in a variety of contexts. Like many organizations, it has used leases to acquire use of equipment and facilities, such as office space. BPA has entered into lease agreements with individual utilities for the construction of specific transmission assets, such as the Hooper Springs substation and associated transmission line. BPA also created an entire program, the lease purchase program, to finance a broad range of transmission capital investments. Under these agreements, BPA designs and manages the construction of assets funded and owned by a third party. The third-party-issued debt is secured by BPA's lease commitment. The debt service on the third-party debt is paid with revenues from BPA's rental payments. Once the lease term ends, BPA can purchase the asset for a nominal fee. This $2.1 billion program has helped BPA preserve access to Treasury borrowing authority.[13] While BPA is not currently forecasting new lease

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[7] *See* Department of Energy Order RA 6120.2 (Sep. 20, 1979), §10d(1).
[8] Transmission System Act, § 2(a), 16 U.S.C. § 838(a) (2020) ("[I]t is desirable and appropriate that the revenues of the Federal Columbia River Power System and the proceeds of revenue bonds be used to further the operation, maintenance, and further construction of the Federal transmission system in the Pacific Northwest.").
[9] *Id.* § 13(a), 16 U.S.C. 838k(a) (2020).
[10] Pub. L. No. 117-58, § 40110 (2021).
[11] Transmission System Act §13(a), 16 U.S.C. 838k(a) (2020).
[12] *Id.* § 11(b)(5), 16 U.S.C. 838i(b)(5) (2020).
[13] Bonneville Power Administration, *Financial Plan Refresh: Grounding Workshop #2*, 25 (Nov. 16, 2021), https://www.bpa.gov/-/media/Aep/finance/financial-plan-refresh/nov-16-workshop-presentation-new.pdf ("Nov. 16 Presentation").

agreements, the lease purchase program is an access to capital tool available should the business need arise.[14]

Prepaid Revenues

Each BPA business unit has made use of prepaid revenues. In 2012, the Power business unit used the "Power Prepay" program, through which power customers were able to purchase blocks of credits to be applied against customer bills through 2028. Four customers purchased $321 million of credits. The funds raised through this offering were used to finance Power capital projects.

The Transmission business unit uses two prepayment programs. The first program is the Large Generator Interconnection Agreements (LGIA) and Small Generator Interconnection Agreements (SGIA). Generators advance funds for the construction of infrastructure at or beyond the point of interconnection. The funds are returned, with interest, to the generator through credits on the generator's monthly bills. Very similar to this is the Line and Load Interconnection Procedure. To mitigate the cost of a stranded investment, customers provide cash deposits to guarantee the cost of construction to meet the needs of new loads. The deposits fund the construction and are returned to customers with interest as credits on monthly bills.

Early Debt Repayment

BPA is required to repay the Federal investment over a reasonable period of years.[15] BPA has—since its creation—often repaid its Federal debt faster than the maximum repayment period.[16] Early repayment can result when non-Federal debt, described below, is refinanced, which frees up capacity in BPA's cost structure to accelerate the repayment of Federal debt. Early repayment is also a result of BPA's repayment methodology, as described below in Section 2.4.

Reserve Financing

BPA has used existing cash on hand, e.g., financial reserves, to finance capital and avoid issuing new debt. From 2006 through 2019, the Transmission business unit reserve financed $15 million per year, for a total of $210 million.[17]

Revenue Financing

BPA also collects revenues through rates to pay for capital investments outright.[18] That is, the cost of directly financing a portion of the capital program with cash is included as a cost to be recovered by BPA's rates. BPA forecast revenue financing 5 percent of its capital

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[14] *Id.*

[15] Bonneville Project Act § 7, 16 U.S.C. § 832f (2020).

[16] Fredrickson *et al.*, BP-22-E-BPA-36, at 26.

[17] Bonneville Power Administration, *Financial Plan Refresh: Debt & Borrowing Authority Grounding Workshop*, 23 (Oct. 19, 2021), https://www.bpa.gov/-/media/Aep/finance/financial-plan-refresh/oct-19-grounding-workshop.pdf ("Oct. 19 Presentation").

[18] *See* Pacific Northwest Electric Power Planning and Conservation Act § 6, 16 U.S.C. 839d (2020) ("Northwest Power Act").

program (called "investment service coverage") and funded construction of the Columbia Generating Station with current revenues in the 1983 rate case.[19] In the 1985 rate case, BPA forecast revenue financing 7.5 percent of its capital program.[20] In the 1987 rate case, BPA forecast revenue financing $39.3 million in FY 1988 and $49.8 million in FY 1989.[21] The 1993 rate case revenue financed Columbia Generating Station capital expenditures with a service life of 10 years or less.[22] In the 1996 rate case, BPA included revenue financing of $37 million per year. [23] This was partially in response to guidance from the U.S. Government Accountability Office and the 1994 House and Senate Appropriations Committees for BPA to reduce its reliance on Treasury borrowing authority by funding a portion of its capital investments through current revenues.[24]

Regional Cooperation Debt

Regional Cooperation Debt (RCD) is debt issued and held by Energy Northwest (EN) that is related to its one operational and two terminated nuclear plants. Through net billing agreements, BPA's contractual commitments support repayment of this debt. In cooperation with EN, the original construction debt has been refinanced, and the maturities extended, as the bonds have come due.[25] By refinancing the debt and extending the maturities, BPA has been able to accelerate the repayment of Federal appropriations and bonds in their place (by using available funds collected in rates to pay off the maturing EN debt that was refinanced). The Energy Northwest Board approved a motion of support to issue up to $3.5 billion in tax-exempt bonds between 2021 and 2030, which will be placed to mature no later than 2044.[26] RCD can be refinanced to support both Power and Transmission business units. Once these bonds are paid off, they cannot be re-issued, and BPA's access to the lower, tax-exempt interest rates for debt management purposes ends.

Other non-Federal Debt

BPA's contractual commitments also support repayment of the debt used to construct two non-Federal hydro-electric projects, the Cowlitz Falls project and the Northern Wasco project. Like RCD, this debt is considered part of BPA's total debt portfolio.

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19 1983 Wholesale Power and Transmission Rate Proposal, Administrator's ROD, WP-83-A-02, at 75, 79 (Sept. 1983).
20 1985 Wholesale Power and Transmission Rate Proposal, Administrator's ROD, WP-85-A-02, at 59, 66 (May 1985).
21 1987 Wholesale Power Rate and Transmission Rate Proposal, Administrator's ROD, WP-87-A-02, at 41-47 (July 1987).
22 1993 Wholesale Power Rate and Transmission Rate Proposal, Administrator's ROD, WP-93-A-02, at 87-88 (July 1993).
23 1996 Wholesale Power and Transmission Rate Proposal, Administrator's ROD, WP-96-A-02, at 74-78 (June 1996).
24 *Id*.
25 Nov. 16 Presentation at 26.
26 *Id.*

2.3 BPA Recovers the Cost of Capital Financing in Rates, Consistent with Statutory Requirements

Regardless of the tools selected, BPA must recover the cost of capital financing decisions through the rates it charges its customers. This follows from Congress's direction that the costs of operating the FCRPS and FCRTS be funded by revenues from power and transmission customers.[27] The Transmission System Act places BPA on a self-financing basis, meaning BPA funds its operations with revenues from power and transmission products and services and does not depend on further appropriations from Congress.[28] BPA is rare among Federal agencies in this regard.

By law, all of BPA's receipts in cash are deposited into the Bonneville Fund, an account held by the Treasury, and BPA uses the amounts in the Bonneville Fund to make cash payments for its operations.[29]

BPA establishes its rates to recover its total costs, in accordance with three general principles:

- to encourage the widest possible diversified use of electric power at the lowest possible rates to consumers, consistent with sound business principles;
- to recover the cost of producing and transmitting such electric power, including the amortization of the capital investment allocated to power over a reasonable period of years; and
- to produce such additional revenues as may be required, in the aggregate with all other revenues of the Administrator, to pay BPA's bond and appropriations obligations to Treasury.[30]

Additionally, the Federal Energy Regulatory Commission (FERC) requires BPA to account for the financial activities of each business unit independently and report the results in each BPA rate filing.[31] All of BPA's costs are, therefore, allocated to the revenue generating business units—Power Services or Transmission Services—and are recovered, in the aggregate, through their respective rates. Through these directives, BPA's customers and their consumers—rather than taxpayers—bear the cost of the FCRPS and FCRTS.

2.4 BPA's Debt Repayment Policies and Practices

For the debt that BPA incurs, BPA's rates must be sufficient to assure repayment of the cost of servicing (e.g., principal and interest) its Federal and non-Federal debt, among other costs. The amount of Federal repayment in a given rate period is required to be consistent with repaying the Federal debt over a "reasonable period of years."[32] Historically, a

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[27] Northwest Power Act § 7(a)(1), 16 U.S.C. § 839e(a)(1) (2020).
[28] Transmission System Act § 11, 16 U.S.C. § 838i (2020).
[29] *Id.* § 11(a), 16 U.S.C. 838i(a) (2020) (establishing Bonneville Fund).
[30] *See* Transmission System Act § 9, 16 U.S.C. § 838g (2020); *see also* Northwest Power Act § 7(a)(1), 16 U.S.C. § 839e(a)(1) (2020); Flood Control Act of 1944, 16 U.S.C. § 825s (2020).
[31] Bonneville Power Administration, 20 FERC ¶ 61,142, at P 61,315 (August 1982); *see also* 25 FERC ¶ 61,140, at P 61,375 (1983); 26 FERC ¶ 61,096 (1984); 28 FERC ¶ 61,325 (1984).
[32] Bonneville Project Act § 7, 16 U.S.C. § 832f (2020).

"reasonable period of years" has been a repayment period of a maximum of 50 years for Power and 35 years for Transmission.

For ratemaking purposes, BPA uses a repayment methodology to determine a schedule of Federal principal payments that satisfies all statutory requirements, ensures timely repayment of the Federal investments, and seeks to establish the lowest level of total debt service—both Federal and non-Federal—over the allowable repayment period.[33] The methodology considers BPA's entire portfolio of debt. The methodology schedules the repayment of Federal debt around the scheduled non-Federal debt service (which has a higher priority of payment) to produce the lowest level of total debt service. As a result, it is common for Federal debt to be retired earlier than its original maturity and earlier than the maximum repayment period. The repayment methodology is not designed to produce results that factor in Treasury borrowing authority constraints, business unit leverage, total outstanding debt, or the optimization of financing choices.[34]

The repayment methodology sets the minimum amount of debt payments (cost) BPA must recover in its revenue requirement used to set its rates. The maximum repayment period for power assets is 50 years. For transmission assets, BPA sets the maximum repayment period at 35 years. Since the BP-14 rate case, BPA has chosen to ensure that Federal repayment is not less than the cash generated by the revenue requirement (*e.g.,* depreciation and amortization expense plus other non-cash adjustments).[35]

The repayment methodology reasonably ensures that BPA sets its rates high enough each rate period to make its payments to the Treasury "over a reasonable period of years."[36] And, because debt service payments on Federal debt are subordinate to payments on non-Federal debt, assuring rates are sufficient to meet Federal debt implicitly assures that rates are sufficient to meet BPA's required payments to non-Federal debt holders. In 2021, BPA made its 38th consecutive annual payment to the Treasury.[37]

2.5 BPA's Debt Management Policies and Practices

Although BPA has a variety of policies and practices that guide its debt management, BPA has not previously adopted a specific policy to guide capital financing decisions. BPA's practice has been to debt finance nearly 100 percent of its capital investments with relatively small, intermittent amounts of revenue financing. Although BPA has, at different times, made use of the various capital financing tools at its disposal, BPA's decisions have largely focused on preserving access to Treasury borrowing authority through refinancing or alternative forms of debt.

2018 Financial Plan

In 2018, BPA released its most recent Financial Plan. As reflected in the figure below, this Financial Plan is organized in order of flexibility, beginning with the foundational and least

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[33] Oct. 19 Presentation at 25; *see U.S. Dep't of Energy – Bonneville Power Admin.*, 141 FERC ¶ 62,234, 64,701 (2012); *see also* Department of Energy Order RA 6120.2.
[34] Oct. 19 Presentation at 25.
[35] Lennox *et al.*, BP-22-E-BPA-20 at 2.
[36] Bonneville Project Act § 7, 16 U.S.C. § 832f (2020).
[37] BPA Annual Report 2021 at 31.

flexible elements (statutory obligations and authorities). These support financial policies and practices, which, in turn, support financial health objectives. These objectives include debt utilization.

BPA Financial Plan Components

The 2018 Financial Plan described the purpose of each objective, the metric BPA would use to analyze the objective, and the target. The purpose of the debt utilization objective was to reduce interest expense and maintain financial flexibility. BPA adopted a debt to asset ratio as the metric to analyze the objective. The target was to achieve a debt to asset ratio of 75-85 percent within 10 years and 60-70 percent in the long term.[38] BPA's actions to achieve this target were guided by the Leverage Policy.

[38] Bonneville Power Administration, 2018 Financial Plan at 11 (Feb. 6, 2018), *available at* https://www.bpa.gov/-/media/Aep/finance/financial-plan/financial-plan-2018.pdf ("BPA 2018 Financial Plan").

Leverage Policy

The Leverage Policy was also established in 2018, and was the first policy effort to address debt as a whole.[39] The Policy set a near-term target that a business unit's leverage ratio could not grow from rate period to rate period. If the ratio was forecast to increase, BPA would take action to ensure the ratio stayed flat on a forecast basis, including adding revenue financing. It was first applied in the BP-20 rate case when $37 million per year of revenue financing was included in the Transmission revenue requirement. However, several issues arose. First, BPA corrected its forecast leverage calculation to include deferred borrowing as debt, to include all capital spending including customer financed investments, and to reflect the effect of asset retirements, the cost of removal, and sale of facilities. Once the forecast formula was corrected, Transmission's leverage ratio was forecast to stay in the 75-77 percent range. The revenue financing amounts expected to trigger from the Policy—which would both preserve borrowing authority and curb Transmission's growing debt profile—would not occur. In a nutshell, the policy tool as designed required correction and, once corrected, would not adequately address the debt management and access to capital issues as intended. Moreover, the Leverage Policy did not create a policy or practice to ensure business units achieved either the 10-year or long-term goals. Those decisions were left to individual rate cases without providing specific policy direction. BPA realized that a more durable, direct policy approach was necessary.

2.6 BPA's Current Debt Portfolio Has Room for Improvement

BPA's financing decisions have resulted in it being highly leveraged with a large amount of debt outstanding, which limits its financial flexibility and ability to ensure a more consistent cost of service over time. As discussed below, the following considerations suggest that additional capital financing policy guidance is prudent: BPA's overall debt outstanding, Transmission's net borrower status, the limited nature of BPA's Treasury borrowing authority, BPA's leverage ratio, industry practice, and the perspective of independent credit rating agencies.

Large Debt Outstanding

At the end of FY 2021, BPA had outstanding $14.1 billion in debt for its power and transmission assets. Approximately $8.3 billion is attributable to BPA's Power business unit. Of this amount, $3.3 billion is Federal debt composed of Treasury bonds and outstanding Federal appropriations repayment obligations, while the remaining $5.0 billion is made up of bonds and similar instruments issued by non-Federal entities (non-Federal debt) and supported by BPA's contractual commitments.[40]

The Federal debt that BPA incurred to support its Power Services has financed the original construction of and replacements, renewals, and improvements to the facilities of the FCRPS, including electric power generation equipment, conservation, and fish and wildlife

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[39] *See* Leverage Policy ROD at 10.

[40] Bonneville Power Administration, *Federal Columbia River Power System (FCRPS): Total Liabilities to Federal and Non Federal Parties as of 9/30/2021*, http://www.bpa.gov/-/media/Aep/finance/outstanding-long-term-liabilities/2021-liabilities.pdf ("FCRPS Liabilities 2021").

mitigation investments. BPA forecasts Power's debt outstanding will gradually decline by almost $1 billion over the next 20 years.[41]

BPA's Transmission business unit accounts for approximately $5.8 billion of the agency's total debt obligation, of which $3.6 billion is in Federal debt, and $2.2 billion is non-Federal debt.[42] Transmission Services' debt is used to sustain program investments in aging transmission equipment and systems, and to expand the existing system to increase capacity and capability.

Transmission's Net Borrower Status

Transmission's debt outstanding has been growing at an unsustainable pace. Over the past 10 years, Transmission's debt has grown by about $2 billion.[43] This trend is forecast to continue. Transmission debt is expected to climb to approximately $8 billion by 2028, and then again to nearly $10 billion by 2040.[44] This growth is driven by Transmission being a net borrower: more debt is issued for Transmission than it repays. Since 2010, Transmission has net borrowed nearly $2 billion, and is forecast to net borrow nearly $4 billion in the next 20 years. Notably, much of this new debt is forecast to fund "sustain" projects—investments in maintaining existing assets—rather than new infrastructure development.[45]

Net borrowing adds significant future fixed costs through interest expense. Transmission's interest expense is projected to increase significantly, from approximately $175 million in FY 2022 to over $300 million in FY 2044.[46] Over the same timeframe, Power's interest expense is projected to decrease from approximately $300 million to $230 million.[47] These fixed costs impact rate pressure and BPA's financial flexibility.

Limited Borrowing Authority

BPA's primary source of debt financing is its U.S. Treasury borrowing authority, which works like a revolving line of credit. The Financial Plan set a policy goal to preserve $1.5 billion of Treasury borrowing authority. In 2020, BPA was projecting that remaining borrowing authority would fall below this threshold by 2024.[48]

The Infrastructure Investment and Jobs Act provided BPA with an additional $10 billion of Treasury borrowing authority, which resolved both BPA's near-term borrowing authority

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[41] Oct. 19 Presentation at 12.
[42] FCRPS Liabilities 2021.
[43] Oct. 19 Presentation at 11.
[44] *Id.*
[45] Bonneville Power Administration, *Comments & Responses* at 34 (May 24, 2022), https://www.bpa.gov/-/media/Aep/finance/financial-plan-refresh/20220524-comment-response-compilation.pdf ("Comment Response Compilation").
[46] Oct. 19 Presentation at 14.
[47] *Id.*
[48] Bonneville Power Administration, *TC-22, BP-22, and EIM Phase III Customer Workshop* at 54-55 (Sept. 29, 2020), https://www.bpa.gov/-/media/Aep/rates-tariff/bp-22/bp-22-meeting-workshops/29sep20-main-tarrif-rates-eim-workshop.pdf.

constraint and the constraint for the foreseeable future. The funding certainty provided by the Act allowed BPA to construct a policy framework that achieves policy objectives over a longer timeframe. While now much larger, BPA's Treasury borrowing authority remains a limited resource that still needs to be prudently managed. The statute specifically required BPA to update its Financial Plan and limited the use of the newly gained borrowing authority to $6 billion through 2027.

High Leverage Ratio

BPA remains highly leveraged. Leverage compares an entity's debt with its revenue-producing assets (debt-to-asset ratio), which is a common metric used in the utility industry to gauge financial health.[49] A higher ratio is generally viewed as less healthy than a lower ratio, because a highly leveraged business has increased fixed costs (principal and interest) that it must repay when they are due and thus less flexibility to address uncertainty and risk.

Overall, at the end of FY 2021, BPA's debt-to-asset ratio is 83 percent.[50] Power is currently at 88 percent, but expected to decline to 60 percent by 2040 based on BPA's repayment methodology and leverage policy near-term target.[51] Transmission is at 77 percent, and projected to remain in the 74-77 percent range though 2040 based on BPA's repayment methodology and leverage policy near-term target.[52]

Industry Practice

While entities have differing asset, economic, and geographic characteristics, it is useful to compare and contrast the practices and financial metrics of entities that are, in some respects, similar to BPA. BPA surveyed regional utilities by reviewing their cost of service studies, official statements for bond offerings, strategic plans, and other publically available documents produced by the utilities, as well as utility training offered by trade associations. BPA noted the vast majority of regional utilities do not borrow for their entire capital program.[53] BPA currently does, which has led to high debt levels and debt-to-asset ratio. Instead, utilities are commonly using revenue to finance capital programs on an annual basis of 40-50 percent, with some utilities even relying on 100 percent revenue financing.[54] Utilities that issue bonds limit their debt financing and explicitly use revenue from rates to finance capital projects.[55]

BPA also considered the practices of the three other Federal power marketing administrations (PMAs).[56] Unlike BPA, the other PMAs all receive annual appropriations.[57]

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[49] *See* BPA 2018 Financial Plan at 11.
[50] BPA Annual Report, 2021 at 16.
[51] Oct. 19 Workshop at 16.
[52] *Id*.
[53] *Id* at 20.
[54] *Id.*
[55] *Id.*
[56] *I.e.,* Western Area Power Administration (WAPA), Southwestern Power Administration (SWPA), and Southeastern Power Administration (SEPA).
[57] Nov. 16 Presentation at 33.

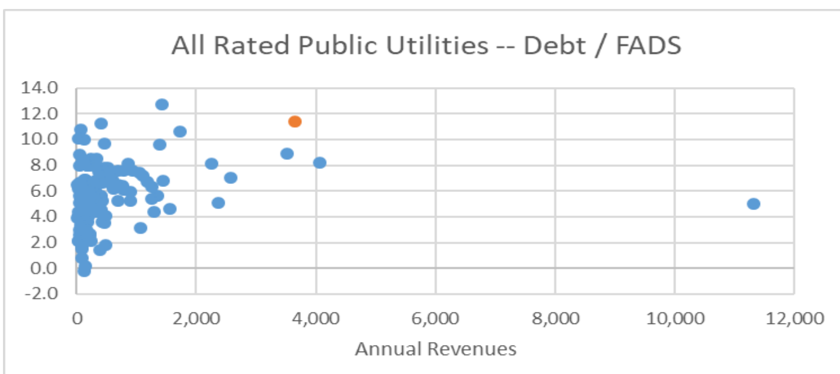
Of the three, only WAPA has Treasury borrowing authority, but it is not to be used to directly finance its own capital construction. None of the other PMAs have non-Federal debt like BPA.[58] They tend to rely on customer financing for capital projects through contractual arrangements, identified as "alternative financing" in their budget documents.[59] Having provided advance funding, these customers then receive credit on their future bills.[60]

Credit rating agencies provide third-party analysis of BPA's overall financial health, in comparison to similar entities, which provide investors with an understanding of the relative risk of investments in various entities. The ratings assigned by the credit rating agencies impact the interest rates that BPA can expect to receive on its non-Federal debt transactions. In general, higher ratings mean lower interest rates and lower costs. The perspective of independent ratings agencies can provide useful comparisons as BPA makes decisions regarding its financial health.

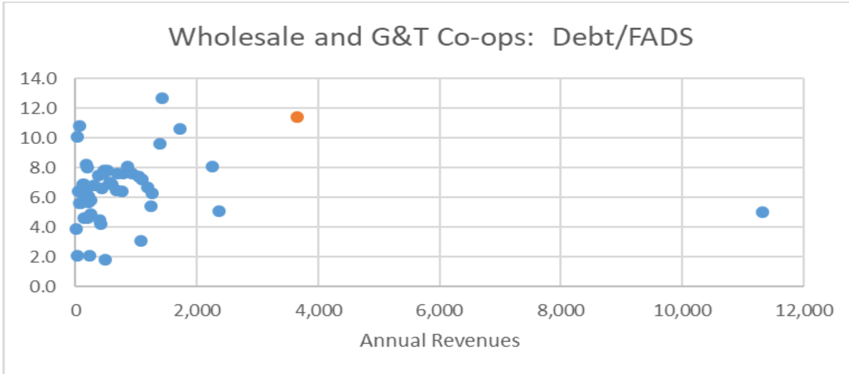
For example, regarding comparators, Moody's includes BPA within the category of public utilities with generation when looking at its version of a debt to asset ratio. BPA is consistently above the medians. While this category has had a median debt-to-asset ratio between 30-45 percent, and the top 50 public utilities with generation have had a ratio between 49-58 percent, BPA has had a ratio of 88-95 percent over the same timeframe.[61]

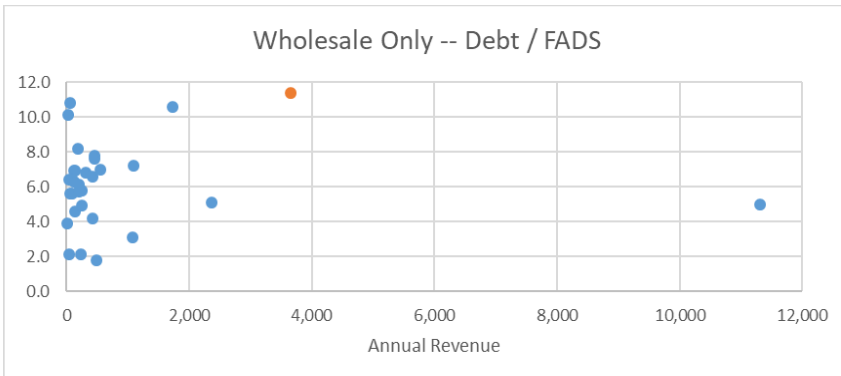
Similarly, Fitch uses a custom metric to assess leverage that compares debt to the funds available for debt service (FADS). Across various categories of utilities, BPA (the orange dot) is an outlier. (See charts below. Higher values on the y axis represent worse leverage.)

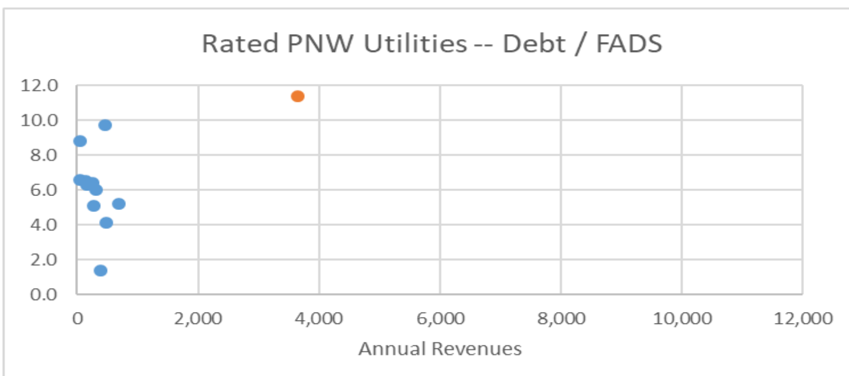
Rating Agency Perspective – Fitch[62]



58 *Id.*
59 *Id.*
60 *Id.*
61 Oct. 19 Presentation at 18.
62 *Id.* at 19. FADS is Funds Available for Debt Service







The credit ratings agencies have seen room for improvement regarding BPA's overall debt outstanding, its capital financing practice, and debt-to-asset ratio. They have seen revenue financing as a credit positive.

In its June 2020 rating, which revised BPA's outlook from "stable" to "negative," Fitch stated:

> Bonneville's already high debt, together with its nearly 100% debt-financed capex plans and weak liquidity profile, could limit its financial flexibility to respond to increased economic uncertainty.[63]

[63] *Id.* at 17.

Moody's June 2021 rating stated:

> Positively, the proposed rates for both power and transmission customers [incorporate] increased revenue financing totaling up to $145 million per year for capital spending although the amount is still modest relative to BPA's consolidated capital spending requirements forecasted at an average of $945 million per year over the FY 2022-2023 period.[64]

Most recently, Moody's April 2022 rating notes that:

> Since 2018, BPA has implemented policies that sought to improve or stabilize BPA's standalone credit strength. Such policies and goals include but are not limited to the establishment of a financial reserve policy, a long-term goal to reduce BPA's debt to asset ratio to around the 60-70% range, and partial rate funding of capital expenditures. We see these goals and policies as an important foundation to the turnaround of BPA's financial performance since 2019 and a material weakening of these credit support features could offset the benefits of the borrowing line increase.
>
> * * *
>
> BPA's rating is likely to be upgraded if BPA maintains or expands its credit supportive goals and policies under its new financial plan, while having access to the larger borrowing line.[65]

2.7 Experience Highlights the Prudency of Establishing a Sustainable Capital Financing Policy

The BP-22 rate case resulted in the adoption of a non-precedential settlement for power and transmission rates for the FY 2022-23 rate period.[66] Among other things, the settlement specified that the Financial Plan Refresh BPA planned to start in Fall 2021 would include "discussion and consideration of issues related to Bonneville's borrowing authority and the use of revenue financing as a source of capital funding."[67]

Prior to the settlement in BP-22, BPA Staff had proposed to revenue finance a portion of each business unit's capital program based on specific circumstances facing each business unit at the time.[68] Several parties raised concerns with Staff's proposal, including that the proposed revenue financing was not guided by a long-term policy.[69] Although the adoption of the settlement made it unnecessary for BPA to address those arguments at the time, a long-term policy could have helped guide Staff's proposals in BP-22 and addressed some of

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[64] *Id*.
[65] Moody's Investor Service, Credit Opinion, Bonneville Power Administration, April 22, 2022 at 2. https://www.bpa.gov/-/media/Aep/finance/rating-agency-reports/moodysfullreportmay2022.pdf.
[66] BP-22 Final ROD, BP-22-A-02, Appendix A, Attachment 1 at 1.
Id. at 3.
[67] *Id.*, Attachment 1 at 1.
[68] Fisher *et al.*, BP-22-E-BPA-15, at 6; Fredrickson *et al.*, BP-22E-BPA-17 at 5.
[69] Coseo *et al.*, BP-22-E-BPA-34, at 8-13.

the concerns raised in the parties' testimony. Those concerns helped inform BPA's approach to the discussion of revenue financing in the Financial Plan Refresh.

2.8 Sustainable Capital Financing Policy Development Public Process

On September 15, 2021, BPA held its Financial Plan Refresh Kick-Off public workshop. This workshop described the scope of this broader initiative, laid out a timeline for the public engagement process, and defined the project objective to ensure BPA's long-term financial goals are supported with the appropriate targets, metrics, and policies.[70] In the area of debt and borrowing authority, BPA stated that the primary focus would be on developing sustainable capital funding and debt management practices.[71]

BPA held a first grounding session on October 19, 2021. This workshop discussed BPA's debt profile, debt-to-asset ratio, and practice regarding capital financing and debt management. Additionally, BPA provided credit rating agencies' perspectives on BPA's leverage, and discussed industry practices.

A second grounding session was held on November 16, 2021. This workshop discussed BPA's practices regarding depreciation, repayment modeling, financing tools, leverage, and the financing practices of the other power marketing administrations. Additionally, in response to a stakeholder request, BPA invited stakeholders to make their own presentations at the January 12, 2022, and January 26, 2022, public workshops.[72]

On January 26, 2022, BPA presented an initial approach for discussion regarding a Sustainable Capital Financing Policy. BPA sought feedback, specifically identifying particular areas of interest.[73] BPA discussed the history surrounding the issue, including key issues to be addressed, and responded to themes BPA had heard from stakeholders.[74] BPA explained its overarching goals and principles, including why these goals are important, how BPA developed its approach, and how BPA anticipated its approach would apply to each business unit.[75]

Also at this workshop, representatives for the Northwest & Intermountain Power Producers Coalition (NIPPC) and Northwest Requirements Utilities (NRU) made presentations.[76] NIPPC presented its perspective on BPA's credit ratings. It stated that deleveraging below 80 percent was unlikely to raise BPA's credit ratings, and suggested

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[70] Bonneville Power Administration, *Financial Plan Refresh: Kick-Off*, 9 (Sept. 15, 2021), https://www.bpa.gov/-/media/Aep/finance/financial-plan-refresh/sep-15-public-kick-off-final-9-13.pdf.
[71] *Id.* at 10.
[72] Nov. 16 Presentation at 4.
[73] Bonneville Power Administration, *Financial Refresh: Public Workshop* (Jan. 26), https://www.bpa.gov/-/media/Aep/finance/financial-plan-refresh/jan-26-workshop-presentation-final.pdf ("Jan. 26 Presentation").
[74] *Id.* at 7-11.
[75] *Id.* at 12-27.
[76] Bart Oosterveld, *Bonneville Power Administration's Financial Plan Refresh and Its Credit Ratings* (Jan. 26, 2022), https://www.bpa.gov/-/media/Aep/finance/financial-plan-refresh/nippc-powerpoint-presentation-26-january-002.pdf ("NIPPC Presentation"); NRU, *NRU's BPA Financial Plan Refresh Policies* (Jan. 26, 2022), https://www.bpa.gov/-/media/Aep/finance/financial-plan-refresh/nru-presentation-at-12622-bpa-workshop.pdf.

alternative entities against which BPA should compare itself. NRU described four financial principles to guide NRU's approach to BPA's Financial Plan refresh, including: targeted utilization of revenue financing; separation of financials by business unit; aiming to improve financial health between 1 and 2 percent annually until debt-to-asset goals are reached; and formalizing decisions through a record of decision.

At the March 23, 2022, public workshop, BPA provided a recap of all Financial Plan Refresh topics, including the Sustainable Capital Financing Policy, and held an open dialogue.[77] Representatives from NIPPC again presented their views on appropriate leverage ratios.

On May 24, 2022, BPA held a public workshop to discuss its draft Sustainable Capital Financing Policy and draft Financial Plan. This started the public comment period. BPA discussed its goals, including why these goals are important; described the approach to calculate default amounts of revenue financing in the Integrated Program Review (IPR) process; described the flexibility in ratemaking and in operations; and identified other key points.[78] BPA held an open dialogue to clarify its proposal, and followed up with a compilation of all BPA's written responses to comments submitted throughout the process,[79] and an example illustrating the calculation of default amounts of revenue financing.

In addition to discussions in the workshops, BPA solicited and responded to written comments following each workshop. Public workshops were also held on January 12, 2022; February 9, 2022; February 23, 2022; and March 9, 2022, to discuss other aspects of the broader Financial Plan Refresh initiative. Snohomish and PPC presented at the March 9 workshop on the topics of capital planning and execution metrics.

The formal comment period on the Sustainable Capital Financing Policy commenced with the issuance of the draft policy, and closed June 16, 2022. BPA received 13 public comments.

3. SUSTAINABLE CAPITAL FINANCING POLICY

The Sustainable Capital Financing Policy (Policy), attached to this ROD as Attachment 1, is comprised of eight sections.

Section 1 provides a broad overview of the Policy, its stated purpose, and the context for the Policy.

Section 2 provides definitions for two concepts used within the Policy: revenue financing, and BPA-funded capital investments.

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[77] Bonneville Power Administration, *Financial Plan Refresh: Public Workshop* (Mar. 23, 2022), https://www.bpa.gov/-/media/Aep/finance/financial-plan-refresh/20222321-Mar-23-Workshop-Presentation.pdf ("Mar. 23 Presentation").
[78] Bonneville Power Administration, *Financial Plan Refresh: Public Workshop*, https://www.bpa.gov/-/media/Aep/finance/financial-plan-refresh/20220524-workshop-presentation.pdf ("May 24 Presentation").
[79] Bonneville Power Administration, *Comments & Responses* (May 24, 2022), https://www.bpa.gov/-/media/Aep/finance/financial-plan-refresh/20220524-comment-response-compilation.pdf ("Comment Response Compilation").

Section 3 describes the scope of the Policy to affect BPA's use of debt and to provide a consistent, long-term framework for managing capital funding practices.

Section 4 identifies the Policy goals, which are to establish a capital financing method that:

1. Moves BPA away from 100 percent debt financing by revenue financing a portion of capital, and
2. Achieves agency and business unit debt-to-asset ratios of no greater than 60 percent by 2040.

Section 5 describes how default amounts of revenue financing will be calculated and describes the flexibility to respond to circumstances in each rate case. The default amount of revenue financing for each business unit will be calculated as follows:

1. The default amount of revenue financing for each business unit will be 10 percent of the IPR[80] loaded capital spending forecast of BPA-funded capital investments that are functionalized to each business unit.
2. However, if 10 percent revenue financing in step 1 results in a business unit debt-to-asset ratio that is greater than 60 percent by 2040 on a forecast basis, the default amount of revenue financing for that business unit will be increased to the lower of:

   (a) 20 percent of the IPR capital spending forecast of BPA-funded capital investment, or

   (b) Incremental revenue financing (compared to the amount of revenue financing included in the prior rate case) of $15 million per year for Transmission Services or $25 million per year for Power Services.[81]

Section 6 describes how revenue financing may be repurposed for liquidity needs under certain circumstances.

Section 7 describes BPA's intent to periodically review the Policy approximately every five years, and states BPA will monitor and annually report its progress toward meeting the Policy goal.

Section 8 describes calculations pertinent to the Policy.

4. RESPONSE TO COMMENTS[82]

4.1 Supportive Comments

Several commenters support various aspects of BPA's decision to adopt the Sustainable Capital Financing Policy. Snohomish County Public Utility District (Snohomish) comments:

> Snohomish supports the goals, approach and flexibility embedded in the Draft Sustainable Capital Financing Policy. Staff's careful consideration of the issue is evident in the following features of the draft policy: matching the timeline

[80] Or its successor.
[81] The amounts in subsection (b) are based on incremental rate impacts of approximately 1 percent for each business unit, on a net-cost basis, which considers savings from avoided interest expense.
[82] All of the comments are available at https://publiccomments.bpa.gov/CommentList.aspx?ID=437.

> between the Integrated Program Review and the Financial Plan Refresh, incorporating flexibility to respond to changing market conditions, commitment to monitoring progress, and more importantly, looking at the Draft Sustainable Capital Financing Policy as a means to achieve a "more stable cost of service over time". The draft policy goes further than the Leverage Policy by providing a roadmap to achieve the objective and sets parameters to mitigate the uncertainty over revenue financing which was the impetus that started the Financial Plan Refresh. As well, Snohomish appreciates the Agency's acknowledgment that continued collaboration is necessary to understand the interplay between the policy and Post-2028 considerations.[83]

Western Public Agencies Group (WPAG) members "appreciate and generally support the approach," and affirm:

> Bonneville has made a compelling case that continuing to debt finance 100% of the capital program is unsustainable. A large portfolio of debt has rate impacts and limits Bonneville's ability to smooth such impacts over time. Having less new debt can work as a hedge against increasing interest rates and provides BPA more financial flexibility to address the uncertainties of a changing operating environment. For these reasons, and subject to the clarifications below, WPAG is supportive of many elements of BPA's revenue financing proposal, including BPA's proposals to [i]nclude a default amount of 10% revenue financing for each business unit with a cap of 20% if achievement of the debt-to-asset ratio goal for 2040 is in doubt; [l]imit the amount of incremental revenue financing from rate period to rate period at $15 million for Transmission and $25 million for Power; [r]epurpose revenue financing to support business line liquidity needs to (i) reduce or eliminate rate-increasing risk adjustment mechanism amounts, e.g., due to the triggering of CRACs or the FRP surcharge, or (ii) restore a business unit's end-of-year reserves for risk to the extent such reserves are expected to be lower than the start-of-year and between 60- and 120-days cash on hand; and [r]etain the flexibility to reduce or eliminate revenue financing for a given rate period to respond to changing circumstances including, importantly, in response to other rate pressures.[84]

NRU commented that "many elements of the revenue financing proposal align with NRU's perspective in several ways: the policy establishes a long-term view with a 2040 target, the approach is consistent and generally, with the exception identified below, would not result in ad hoc revenue financing proposals, and the policy includes an element to simplify rate surcharges or refunds with the proposal to repurpose funds in the operational period to ensure business line liquidity."[85] Public Power Council (PPC) determined "[t]he current BPA proposals substantively address most of the sideboards and considerations in PPC's

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83 Snohomish Comments at 1.
84 WPAG Comments at 1.
85 NRU Comments at 1.

initial comments, including prioritization of reserves for risk mitigation and the need for openness to changes if needed to accommodate developments in the post-2028 process."[86] Alliance of Western Energy Consumers (AWEC) "supports BPA's approach to flexibility with prioritizing liquidity, particularly the ability to redirect cash to mitigate the size of a surcharge."[87]

Powerex states:

> The draft policy lists several negative consequences of the status quo approach, such as higher interest expenses, lower financial flexibility, increased likelihood of credit downgrades, and rate instability. Powerex appreciates Bonneville's acknowledgment and consideration of these factors and generally supports actions that result in lower and stable transmission rates.[88]

Several commenters expressed appreciation for BPA's process in developing the draft policy. NIPPC *et al.* state:

> The Financial Plan Refresh of [BPA] has been a valuable process for customers and other stakeholders to understand BPA's financial practices and potential revisions to the current Financial Plan. The undersigned organizations appreciate the time that BPA Staff has taken to host workshops, consider public comments, and develop proposals to revise the current Financial Plan. Adopting a reasonable and disciplined plan to maintain the agency's financial strength is an important responsibility of BPA.[89]

AWEC "acknowledges and appreciates BPA's continued commitment to communication and transparency with stakeholders throughout the Financial Plan Refresh process."[90] Avangrid *et al.* "appreciate the opportunity to discuss with BPA and its customers the BPA Financial Plan Refresh and to provide additional comments and feedback after each workshop."[91] Powerex "appreciates Bonneville's efforts over the past ten months to address and update its 2018 financial plan and to set forth a policy on the use of revenue financing to fund Bonneville's projected capital expenditures through 2040."[92] NRU "appreciates BPA's efforts to refresh its Financial Plan and Sustainable Capital Financing Policy and recognizes the considerable staff time devoted to educational workshops and the development of the Draft."[93]

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[86] PPC Comments at 1.
[87] AWEC Comments at 4.
[88] Powerex Comments at 1.
[89] NIPPC *et al.* Comments at 1.
[90] AWEC Comments at 1.
[91] Avangrid *et al.* Comments at 1.
[92] Powerex Comments at 1.
[93] NRU Comments at 1.

4.2 Objections and Concerns

4.2.1 Overview

Stakeholders also raise a number of objections and concerns with the proposed Sustainable Capital Financing Policy. These comments generally fall into four categories:

- Concerns with revenue financing as a tool in general;
- Concerns with the Policy's goals;
- Concerns with the Policy's rate impact; and
- Concerns with the Policy's implementation.

BPA responds to these comments below.

4.2.2 Revenue Financing in General

Issue 4.2.2.1

Whether the Sustainable Capital Financing Policy's revenue financing violates the statutory standard to establish rates "with a view to encouraging the widest possible diversified use of electric power at the lowest possible rates to consumers consistent with sound business principles."[94]

Public Comments

M-S-R Public Power Agency (MSR) objects that the revenue financing called for in the Policy "raises costs on a net and absolute basis," and will result in rates being raised "above the lowest possible level without a benefit to customers, and without a supportable business principle."[95] MSR describes the Policy as "an aggressive shift from BPA's existing Leverage Policy,"[96] and asserts the Policy "imposes $1.7 billion in unnecessary costs to consumers."[97] MSR compares the cost of revenue financing against interest savings to assert, "the financial benefits of the revenue financing are less than their cost to customers . . . ."[98] In the near term, MSR objects to the Policy's impact on the BP-24 rate case.[99] MSR argues, "the Draft Policy would add at least $55 million to Transmission's annual revenue requirement, and $65 million to Power's annual revenue requirement . . . due to the use of revenue financing instead of debt financing [that] will not improve service and will not add any new facilities."[100] "Put simply," MSR states, "revenue financing costs consumers more than debt financing, even considering avoided interest."[101] MSR argues

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[94] Transmission System Act § 9, 16 U.S.C. § 838g (2020); *see also* Northwest Power Act § 7(a)(1), 16 U.S.C. § 839e(a)(1) (2020); Flood Control Act of 1944, 16 U.S.C. § 825s (2020).
[95] MSR Comments at 12.
[96] *Id.* at 2-3.
[97] *Id.* at 4.
[98] *Id.* at 5.
[99] *Id.*
[100] *Id.*
[101] *Id.*

that revenue financing, when Treasury borrowing authority is available, is contrary to BPA's statutory directives.[102]

MSR asserts that revenue financing "suggests that BPA has abandoned its commitment to cost-based rates."[103] Avangrid *et al.* also argue that BPA has not established that revenue financing is appropriate "particularly in light of . . . the statutory requirement that BPA establish rates to recover its costs . . . ."[104]

<u>Evaluation</u>

Among several statutory rate directives, BPA's rates are set "with a view to encouraging the widest possible diversified use of electric power at the lowest possible rates to consumers consistent with sound business principles."[105] MSR contends that the Sustainable Capital Financing Policy violates this directive because BPA would be, in MSR's view, "impos[ing] $1.7 billion in unnecessary costs to consumers."[106] MSR is incorrect.

First, the Sustainable Capital Financing Policy adopted by this decision is not establishing any rates or costs. This Policy, as described more fully in Issue 4.2.5.3, will inform the amount of revenue financing BPA Staff will include in its initial proposal in a given rate case. Any party to the rate case will be free to present arguments and evidence in support of another amount, including zero. The Policy only provides an input into BPA's ratemaking, and that input may change as a result of the rate-setting process. Consequently, although adoption of the Policy is a reasonable business decision, and implementation of the Policy is expected to result in an overall net benefit, BPA need not demonstrate that this Policy decision will result in costs or rates that are consistent with the "lowest possible rates consistent with sound business principles" directive.

Second, MSR's more general contention that the Policy violates the business-oriented construct of BPA's statutory authorities is also misplaced. The general statutory directive that BPA set its rates "with a view to encouraging the widest possible diversified use of electric power at the lowest possible rates to consumers" is tempered by the phrase "consistent with sound business principles."[107] Congress did not define "sound business principles." BPA has broad discretion to best determine how to operate consistent with the "business-oriented philosophy" reflected in BPA's statutes.[108] Businesses often make financial decisions that have short- and long-term impacts on their operations. Prioritizing lower rates today may produce higher rates in the future, and vice versa. These

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102 *Id.* at 8.
103 *Id.* at 12.
104 Avangrid *et al.* Comments at 1.
105 Transmission System Act § 9, 16 U.S.C. § 838g (2020); *see also* Northwest Power Act § 7(a)(1), 16 U.S.C. § 839e(a)(1) (2020); Flood Control Act of 1944, 16 U.S.C. § 825s (2020). (20162020).
106 MSR Comments at 4.
107 Transmission System Act § 9, 16 U.S.C. § 838g (2020); *see also* Northwest Power Act § 7(a)(1), 16 U.S.C. § 839e(a)(1) (2020); Flood Control Act of 1944, 16 U.S.C. § 825s (2020). (20162020).
108 *See Ass'n of Pub. Agency Customers v. Bonneville Power Admin.*, 126 F.3d 1158, 1171 (9th Cir. 1997) ("The statutes governing BPA's operations are permeated with references to the 'sound business principles' Congress desired the Administrator to use in discharging his duties. Thus, although Congress did not prescribe the parameters of the Administrator's authority, it granted BPA an unusually expansive mandate to operate with a business-oriented philosophy.") (internal citations omitted).

considerations are not unique to BPA, as every individual and business must inherently make choices about the financial tradeoffs between the short term and the long term. The question BPA faces is whether there are business-related reasons to increase near-term costs to achieve long-term savings or achieve other benefits, such as financial flexibility and the ability to ensure a more consistent cost of service over time. As described below, BPA finds there are sound business reasons to adopt the Policy and potentially include costs in rates in the near term to achieve benefits for the long term. As discussed in Issue 4.2.4.1, BPA considered the Policy's potential rate impact, and designed it to make progress towards BPA's long-term goal over a 20-year horizon, with no greater than about 1 percent incremental rate impact per rate period. This Policy is a reasonable business decision that will support BPA in establishing rates at the lowest possible rates to consumers consistent with sound business principles.

Third, contrary to MSR's assertion that "the financial benefits of the revenue financing are less than their cost to customers,"[109] revenue financing results in an overall net *benefit* when compared to debt financing. Foundational to MSR's concerns with BPA's decision to adopt the Policy is its view that, overall, revenue financing increases the costs to BPA's customers without any appreciable long-term benefit. For support, MSR calculates the total projected revenue financing through BP-40, subtracts the projected interest savings, and argues that this delta represents a net and absolute cost increase.[110]

MSR's calculation ignores the fact that the principal amount of capital investments remains the same whether BPA finances them with debt or revenue financing. Revenue financing is not incremental to BPA's actual costs; it does not change the overall size of BPA's capital program at all. The projected $1.7 billion cited by MSR would be incurred regardless of how BPA finances the projects. Instead, revenue financing reduces BPA's overall interest expense because it avoids the use of debt to finance that portion of capital investments. *Any* interest expense savings represents a net benefit due to revenue financing. Essentially, the decision between revenue financing and debt financing is whether to pay now, or pay later with interest.

When viewing a single rate period in isolation, revenue financing does have a "net cost" compared to repaying the minimum annual principal and interest payments on new debt. This is also the case with student loans and other forms of debt; there would be a near-term "net cost" to paying tuition upfront as compared to a minimum debt repayment amount, but interest expense on top of tuition makes debt a more expensive option overall. BPA presented analysis on the near-term cost in considering the rate impact of its policy proposal.[111] However, revenue financing results in an overall net benefit by avoiding interest expense.

BPA projects these interest savings to be significant. Each decision to revenue finance has interest savings compared to the interest that would otherwise accrue over the life of a bond (which is a type of debt instrument). For example, a $40 million bullet bond with a

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109 MSR Comments at 5.
110 *Id.* at 4, n.6.
111 Jan. 26 Presentation at 22, 26.

30-year maturity and an interest rate of 3 percent will incur $36 million of interest over its life, which would be avoided if revenue financing were used in lieu of the debt. In the context of an established policy to regularly revenue finance a portion of BPA's capital program, these savings compound quickly. Between now and 2040, BPA projects that revenue financing by Power and Transmission could save about $900 million.[112]

These projected savings could increase. The savings estimates are based on low forecasted interest rates, around 3.75 percent. If interest rates increase, the savings will grow.In general, a scenario of increasing and higher rates going forward is more likely than continued low or decreasing rates. Moreover, BPA's interest rates are market-based rates and as such have followed the overall historically low rates seen in the market over the past 10 years. As a case in point, the weighted average interest rate (WAI) on BPA's bonds issued to the U.S. Treasury followed the downward interest rate trend in the early 2000s through the past year:

- FY2000 WAI = 6.7 percent;
- FY2010 WAI = 4.4 percent;
- FY2020 WAI = 2.6 percent.[113]

The current low interest rate environment can change as evidenced by the Federal Reserve Board increasing benchmark interest rates several times between March and August 2022. There is the possibility that interest rates could continue to increase over the next rate period. A specific real-time example has been the increase in BPA's borrowing rate from the U.S. Treasury over the past year. At the start of FY 2022, a 30-year bond would have received an interest rate of 2.38 percent,[114] whereas a 30-year bond issued at the beginning of July 2022 would have received an interest rate of 3.92 percent.[115] This represents a 154 basis point increase (about 1.5 percentage points) in rates over the past nine months alone.

To reiterate, revenue financing at the levels anticipated under this Policy, using a very conservative estimate, has the potential to save BPA and its ratepayers hundreds of millions of dollars in avoided interest expense. If interest rates continue to climb, as appears likely, the savings will only increase. This represents an overall net savings to customers, not a net cost.

Even with the revenue financing proposed in the Policy, BPA expects to continue to heavily rely on debt to finance its capital program. Under this Policy, BPA still anticipates financing approximately 80-90 percent of its capital program with debt. BPA understands that it must balance competing considerations such as near-term rate impact, competitiveness, industry practice, rate stability, intergenerational equity, and sound business principles, and did so in developing the features of this long-term Policy.

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112 Comment Response Complication at 58.
113 *See* Bonneville Power Administration, *Outstanding Long-Term Liabilities*, https://www.bpa.gov/about/finance/debt-management/outstanding-long-term-liabilities.
114 E-mail from Federal Financing Bank, U.S. Dep't of Treasury, to the BPA Treasury organization (July 1, 2022, 07:05 PST) (on file with author).
115 E-mail from Federal Financing Bank, U.S. Dep't of Treasury, to the BPA Treasury organization (Oct. 1, 2021, 07:10 PST) (on file with author).

The Policy's use of revenue financing is consistent with cost-based rates. Regardless of its financing decision, the costs recovered in BPA's rates are BPA's cost of financing its capital investments. The revenue generated by rates is used to pay for actual assets. While revenue financing has near- and long-term implications on the overall level of BPA's rates, the costs recovered through revenue financing are BPA's costs. The difference is one of timing: does BPA pay for the asset now (without interest) or pay over time (and incur interest expense).

BPA also disagrees with MSR's characterization of the Policy as an "aggressive shift" from the Leverage Policy.[116] While the Leverage Policy contained a near-term target to not allow a business unit's leverage to increase rate period to rate period, the Leverage Policy also contained a long-term target to achieve leverage ratios of 60-70 percent. The projected Transmission revenue financing for BP-24 is about the same under the Sustainable Capital Financing Policy. Maintaining flat leverage for Transmission under the Leverage Policy would require revenue financing $56 million per year. BPA expects the default amount of revenue financing under the Sustainable Capital Financing Policy will be $55 million per year. In any event, as described in Section 2.5, the two policies serve different objectives.

Finally, BPA notes that the materials shared with customers anticipated default amounts of revenue financing for BP-24 of $39 million per year for Power and $55 million per year for Transmission.[117]

Decision

The Sustainable Capital Financing Policy's revenue financing is consistent with BPA's mandate to operate with a business-oriented philosophy and will support establishing rates "at the lowest possible rates to consumers consistent with sound business principles."

Issue 4.2.2.2

Whether revenue financing is appropriate in light of BPA's available Treasury borrowing authority.

Public Comments

Several commenters argue that revenue financing is not necessary given BPA's available Treasury borrowing authority.

AWEC states: "[I]t is still unclear why revenue financing is necessary or ideal" given the recent increase in BPA's Treasury borrowing authority.[118] AWEC notes that "BPA's capital funding concerns were a main driver for its interest in revenue financing initially,"[119] and that BPA has stated that flexibility and future funding certainty of additional borrowing

[116] MSR Comments at 2.
[117] Bonneville Power Administration, *Illustrating the Calculation of Default Amounts of Revenue Financing*, https://www.bpa.gov/-/media/Aep/finance/financial-plan-refresh/20220524-capital-financing-policy-example.pdf.
[118] AWEC Comments at 2.
[119] *Id.*

authority means access to capital funding is no longer a near-term concern.[120] Therefore, AWEC recommends BPA "decline to move forward with revenue financing as part of its Financial Plan Refresh at this time."[121]

PNGC Power (PNGC) "is not fundamentally opposed to the concept of revenue financing."[122] However, PNGC "do[es] not think the current BPA proposal is necessary or justified considering BPA's increase in borrowing authority and substantially better financial situation compared to just a few years ago."[123]

Avangrid *et al.* argue that BPA has not established that revenue financing is appropriate "particularly in light of . . . the recent increase in BPA's Federal borrowing authority and BPA's unique borrowing authority flexibility . . . ."[124]

MSR argues that "[t]he proposed policy of requiring revenue financing as part of each rate case is unnecessary because BPA's own analysis shows BPA will have sufficient borrowing authority to meet its capital needs."[125] According to MSR, "[t]he revenue financing BPA would impose under the Draft Policy fails to make the best use of a unique resource (borrowing authority) provided to BPA by Congress, particularly in this period of high inflation."[126]

MSR argues that revenue financing violates the Infrastructure Investment and Jobs Act.[127] Further, MSR argues that failing to use available Treasury borrowing authority to 100 percent debt finance BPA's capital program is contrary to BPA's statutory directives.[128] MSR states: "Sound business practices must consider the unique characteristics of BPA's borrowing authority when determining the benefits and burdens of 100% debt financing, particularly when doing so is forecasted to leave $5 billion of BPA's borrowing authority available after BP-40,"[129] and concludes that "[a]dding costs in the form of revenue financing when Congress provided BPA with sufficient borrowing authority to fund the system is not a sound business practice."[130]

Other commenters support BPA's goal to move away from 100 percent debt financing by revenue financing a portion of capital. Snohomish "supports the goals, approach and flexibility embedded in the Draft Sustainable Capital Financing Policy," including BPA's "looking at the Draft Sustainable Capital Financing Policy as a means to achieve a 'more stable cost of service over time.'"[131]

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[120] *Id.*
[121] *Id.*
[122] PNGC Comments at 1.
[123] *Id.*
[124] Avangrid *et al.* Comments at 1.
[125] MSR Comments at 3.
[126] *Id.* at 5.
[127] *Id.* at 3.
[128] *Id.* at 8.
[129] *Id.*
[130] MSR Comments at 12.
[131] Snohomish Comments at 1.

WPAG states:

> Bonneville has made a compelling case that continuing to debt finance 100% of the capital program is unsustainable. A large portfolio of debt has rate impacts and limits Bonneville's ability to smooth such impacts over time. Having less new debt can work as a hedge against increasing interest rates and provides BPA more financial flexibility to address the uncertainties of a changing operating environment. [132]

Evaluation

BPA agrees that it is not in the same crisis situation it was in during the BP-22 rate period. We are no longer facing the near-term reality of depleting available borrowing authority and revenue financing very large amounts out of necessity. As MSR cites, BPA's analysis showed that, even with a 25 percent increase in capital spending and no added revenue financing, BPA projects adequate Treasury borrowing authority through 2042.[133]

BPA disagrees, however, that it should only revenue finance from a place of crisis. Even within the BP-22 rate case, Staff noted, "increased borrowing authority would do nothing to address BPA's concerns about relying on 100 percent debt financing or Transmission's growing debt outstanding issue."[134] As discussed in Section 2.6, BPA's large debt outstanding, Transmission's net borrower status, BPA's high leverage ratio, and the example of industry practice, all affirm that BPA would benefit from a more strategic approach to debt management and capital financing. This is in addition to the necessity of prudently managing the limited resource of BPA's Treasury borrowing authority.

BPA need not wait for a crisis before taking prudent steps to manage its debt profile. As discussed in Issue 4.2.2.3, establishing a policy guides every rate period to contribute in a defined and equitable manner over time to obtain the long-term benefits of revenue financing. This prevents placing the burden of another crisis on some future rate case, and results in a more stable cost of service over time.

MSR argues that the existence of available Treasury borrowing authority renders any decision to revenue finance as inconsistent with sound business principles.[135] BPA disagrees. Nothing in BPA's statutes requires it to debt finance as much as possible, with revenue financing reserved as a tool of last resort only after all other financing options have been depleted. In the Leverage Policy ROD, BPA "[found] no statutory impediment to taking prudent steps (such as revenue financing) to preserving its own long-term financial health by managing its leverage to a reasonable level."[136]

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[132] WPAG Comments at 1.
[133] MSR Comments at 4 (citing Mar. 23 presentation at 8).
[134] Fredrickson *et al.,* BP-22-E-BPA-36, at 40.
[135] MSR Comments at 8.
[136] Leverage Policy ROD § 4.3.5.1.

BPA included revenue financing in its 1983,[137] 1985,[138] 1987,[139] 1993,[140] and 1996[141] rate cases, despite the existence of available Treasury borrowing authority. The latter was partially in response to guidance from the U.S. Government Accountability Office and the 1994 House and Senate Appropriations Committees for BPA to reduce its reliance on Treasury debt by funding a portion of its capital investments through current revenues.[142] Relatedly, BPA has—since its creation—often repaid its Federal debt faster than the maximum repayment period.[143] Revenue financing can be seen as a variation on the theme of financing assets in a shorter period of time than a bond schedule would require. From a rates perspective, revenue financing has the same impact as early debt repayment.

We also note that, along with the recent increase in Treasury borrowing authority, the statute specifically required BPA to update its Financial Plan and limited the use of the newly gained borrowing authority to $6 billion through 2027.[144] BPA should prudently manage this resource. MSR notes that the Act also states:

> The Administrator shall . . . to the maximum extent practicable, implement those policies that would be expected to be consistent with the lowest possible power and transmission rates consistent with sound business principles.[145]

As discussed in Issue 4.2.2.1, this Policy is a reasonable business decision that will support BPA in establishing the lowest possible rates to consumers consistent with sound business principles.

It is consistent with sound business principles to not solely rely on debt financing. Using debt for all of its capital investments would require BPA to have a debt-to-asset ratio of 100 percent in perpetuity. It is not common for utilities to solely rely on debt financing for their capital investments, and BPA's survey of industry practice bore this out.[146] Both private and public utilities take action to reduce their debt load, and no authority requires BPA to 100 percent debt finance its capital program. A long-term policy to guide decisions to take out less debt is consistent with BPA's statutory mandate to set rates as low as possible consistent with sound business principles. BPA recognizes that Treasury borrowing authority is an incredibly valuable tool, and financing decisions must balance

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137 1983 Wholesale Power and Transmission Rate Proposal, Administrator's ROD, WP-83-A-02, at 75, 79.
138 1985 Wholesale Power and Transmission Rate Proposal, Administrator's ROD, WP-85-A-02, at 59, 66.
139 1987 Wholesale Power and Transmission Rate Proposal, Administrator's ROD, WP-87-A-02, at 41-47.
140 1993 Wholesale Power and Transmission Rate Proposal, Administrator's ROD, WP-93-A-02, at 87-88.
141 1996 Wholesale Power and Transmission Rate Proposal, Administrator's ROD, WP-96-A-02, at 74-78.
142 *Id.* at 76 ("It is especially important to reiterate that Congress expects BPA to make efforts to achieve stability and flexibility and to reduce its reliance on Treasury debt by funding a portion of its capital investments through current revenues. . . . In a 1994 Senate Appropriations Committee report, the Senate stated, 'BPA's reliance on debt financing for capital programs is risky and leaves the agency with little flexibility in meeting future challenges.' . . . It was the intent of Congress that borrowing from Treasury for capital improvements was to augment available operating funds not replace them totally.")
143 Fredrickson *et al.,* BP-22-E-BPA-36, at 26.
144 Infrastructure Investment and Jobs Act, Pub. L. No. 117-58, § 40110.
145 *Id.*; MSR Comments at 3.
146 Oct. 2021 Presentation at 20-22.

the considerations discussed in this ROD. This balance, however, is a very different analysis than a requirement to only revenue finance as a last resort.

Decision

Revenue financing is an appropriate tool, even when Treasury borrowing authority is available.

Issue 4.2.2.3

Whether the Sustainable Capital Financing Policy inequitably allocates costs to current ratepayers versus future ratepayers.

Public Comments

NIPPC *et al.* argue that the draft Financial Plan, and implicitly the Sustainable Capital Financing Policy, does not adequately consider "intergenerational equity, by matching the financing of long-lived assets to their useful life."[147] They argue BPA's Policy will "require current ratepayers to pay proportionally more upfront for assets that will benefit future generations of ratepayers."[148]

Powerex argues that the draft policy fails to acknowledge that BPA is asking customers to bear significantly higher rates to fund long-life assets that will benefit future customers, which raises concerns about inter-generational equity.[149] Powerex describes the impact of the Policy: "Instead of amortizing the costs of the assets over 50 years if funded through debt, for example, Bonneville is essentially asking customers to fund those assets over 9 rate periods, or just 18 years."[150]

Avangrid *et al.* argue that BPA has not established that revenue financing is appropriate "particularly in light of . . . the lack of intergenerational equity that results from BPA revenue financing assets . . . ."[151]

MSR argues that "[f]unding assets with debt with a repayment term equal to the life of the asset imposes repayment obligations on those using the asset," and that "[p]aying off assets over their useful life is a common, fundamentally sound practice."[152] In contrast, MSR asserts, revenue financing "creates generational inequity, with ratepayers in 2022 funding 100% of the cost of assets that customers will use for 35 or more years."[153] MSR also argues that "[r]evenue financing violates cost causation by requiring customers to pay all the costs of assets when they will not use all the value of the asset."[154] MSR states revenue

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147 NIPPC *et al.* Comments at 3.
148 *Id.*
149 Powerex Comments at 2.
150 *Id.*
151 Avangrid *et al.* Comments at 1-2.
152 MSR Comments at 8-9.
153 *Id.* at 9.
154 *Id.*

financing can only be appropriate if the asset's useful life is one year or less and the asset is expensed.[155]

MSR characterizes BPA's position as being "that it is inequitable to use 100% debt financing because it imposes debt repayment obligations on future generations of ratepayers."[156] MSR disagrees with this position because "future generations of ratepayers will get to use the assets funded by the debt, so there is no inequity in requiring them to repay a portion of the cost of the assets through debt repayment."[157]

The Oregon Public Utility Commission (OPUC) and the Washington Utilities and Transportation Commission (WUTC) state that "this proposal would reduce BPA's debt ratio in a way that potentially shifts considerable costs onto the transmission customers of investor-owned utilities . . . ."[158] Because the Policy will not change the size of BPA's overall capital program, and does not shift costs between customer groups, BPA understands this argument to refer to the temporal shift of revenue financing's near-term impact.

Evaluation

Commenters' core argument is that revenue financing violates the principle of intergenerational equity, because the cost of a long-lived asset is recovered in one rate case and not spread over the life of the asset to all future ratepayers that will benefit from the asset. This suggests that the principle of intergenerational equity requires financing all assets with debt extended to its maximum maturity to match the asset's useful life. BPA disagrees.

The principle of intergenerational equity is not a mechanical requirement, but one of several potentially competing considerations to be balanced in setting rates. Other principles and considerations include revenue sufficiency, understandability, feasibility, fairness, stability, simplicity, efficiency, effectiveness, and acceptance. BPA has balanced intergenerational equity considerations in prior decisions involving revenue financing.[159] The benefits of revenue financing must be considered along with concerns regarding intergenerational equity.

The commenters' rigid definition of intergenerational equity is belied by utility practice. The principle has not precluded other utilities from revenue financing. Bond maturities are largely a result of market demand; they are not tied to the asset's useful life. Utilities are

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155 *Id*.
156 *Id.*
157 *Id.*
158 OPUC and WUTC Comments at 1.
159 *See, e.g.,* 1996 Wholesale Power and Transmission Rate Proposal, Administrator's Record of Decision, WP-96-A-02, at 74-78 ("BPA believes that, on balance, the benefits of increased financial stability and flexibility far outweigh the benefits of ensuring near term intergenerational equity."); Leverage Policy ROD at 55 ("The choice between debt financing and revenue financing involves tradeoffs between the goals of intergenerational equity, and Bonneville's goals of financial flexibility and health. Bonneville agrees that intergenerational equity is an important consideration when considering its policies. However, on balance, Bonneville finds that it is reasonable at this time to pursue financial flexibility and health through the Leverage Policy.").

commonly focusing cash contributions (revenue financing) for capital programs on an annual basis in the range of 40-50 percent, with some utilities even relying on 100 percent revenue financing.[160] BPA is unaware of utilities intentionally extending their debt to its maximum maturity to match the useful life of their assets, and the prevalence of utilities with leverage ratios significantly below 100 percent implies that such utilities are, in fact, recovering their financing costs over a shorter period of time than the assets' useful lives. The principle of intergenerational equity does not require a utility to forego opportunities to prudently manage its long-term costs and financial flexibility to ensure that everyone pays the same amount. To the contrary, BPA makes sound business decisions about capital financing in response to business considerations such as interest rates, the timing of bond maturities, and other important financing elements, with significant cost savings to BPA and its customers.

Further, intergenerational equity should be evaluated from the perspective of the capital portfolio as a whole rather than focusing on individual assets. BPA finances its capital program on a portfolio basis, with revenue financing occurring in conjunction with debt issuances, refinancing, and debt repayment. In each rate period, rate payers contribute to finance a portion of the capital portfolio from which they benefit, and by regularly revenue financing a portion, the overall cost of the portfolio will be lower.

Revenue financing in the context of an established policy significantly alleviates concerns with intergenerational equity. MSR misunderstands BPA's position on this point. In the January 26 Workshop, BPA discussed feedback it had received from stakeholders, including concerns with intergenerational equity.[161] In response, BPA stated that it "considered intergenerational equity by having a long-term policy, helping to ensure a more consistent debt service level over time."[162] BPA does not believe, as MSR asserts, "that it is inequitable to use 100% debt financing," but rather that revenue financing has benefits that should be considered. It can be equitable to 100 percent debt finance, but long-term costs will be higher, and BPA will sacrifice financial flexibility. It can also be equitable, in the absence of a policy, to make a revenue financing decision based on all the circumstances including balancing intergenerational equity considerations. An established policy, however, helps promote consistency in BPA's rate proposals from rate case to rate case, so that customers in each rate period contribute a reasonable amount to achieve the long-term benefits of revenue financing and help ensure a more consistent debt service level over time. While this Policy includes flexibility to deviate from the Policy's default amount of revenue financing based on the circumstances of a given rate case, intergenerational equity considerations would play a role in such decisions.

In the BP-22 rate case, several stakeholders argued that BPA's revenue financing should be made in the context of a long-term policy,[163] and one customer group argued, in intergenerational equity terms, that BPA's revenue financing proposal did not have a long-

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160 Oct. 19 Presentation at 20.
161 Jan. 26 Presentation at 9.
162 *Id.* at 11.
163 Coseo *et al.,* BP-22-E-BPA-34, at 8-13.

term plan in place to equitably assign revenue financing responsibilities between current and future generations.[164] While BPA Staff maintained that BPA could revenue finance on a case-by-case basis, Staff agreed that its proposals could have been aided by a long-term policy.[165] Under the Sustainable Capital Financing Policy, rates in each rate period are expected to recover the cost of revenue financing 10 percent of a business unit's capital program. A long-term policy that consistently applies the same rate of revenue financing also creates equity over time, because each generation will contribute proportionately the same amount of cash to finance the capital program. In order to achieve long-term objectives, additional revenue financing is projected for Transmission. This Policy takes measured steps to achieve these objectives over the course of 20 years, rather than waiting until BPA is in a crisis that could entail placing a large burden on a single rate period. The Policy balances benefits like lower costs, increased financial stability, and financial flexibility with near-term rate impacts and intergenerational equity.

Decision

The Sustainable Capital Financing Policy is equitable in its consideration of current and future ratepayers.

Issue 4.2.2.4

Whether revenue financing's cost of capital is higher than debt financing.

Public Comments

MSR argues that revenue financing has a higher cost of capital than debt financing, and therefore "customers are better off, and rates are lower, when BPA uses federal debt to fund capital than if BPA utilizes revenue financing."[166] First, MSR points to the "net cost" in BPA's January 26, 2022 workshop presentation as evidence that BPA's "use of revenue financing to reduce interest expense will result in significantly increased costs to BPA's customers and the region."[167]

Second, MSR argues:

> The only way that replacing additional borrowing with increased revenue financing can reduce the cost of capital is if revenue financing has a lower cost of capital than debt. Viewing revenue financing as a non-traditional form of equity capital, it should have a higher cost of capital, not a lower cost of capital. Thus, we would expect that lower leverage (and higher non-traditional equity) would result in a higher cost of capital.[168]

MSR "disagree[s] that customers can finance capital assets without a cost,"[169] and objects that BPA "does not take into account the universal cost of money . . . ."[170]

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164 *Id.* at 23.
165 *Id.* at 10, 23-24.
166 MSR Comments at 5-6.
167 *Id.* at 6.
168 *Id.*
169 *Id.*
170 *Id.* at 5.

Evaluation

As discussed in Issue 4.2.1, the "net cost" referred to by MSR was used to evaluate the near-term rate impact of BPA's initial policy approach. Interest expense savings represent an overall net benefit to revenue financing.

MSR's arguments rest on a flawed syllogism. MSR notes that most transmission-owning utilities do not 100 percent debt finance their capital program. "[M]ost transmission-owning utilities use a mix of debt and equity to fund capital."[171] MSR reasons that:

> Since equity often has a higher cost of capital than debt;
> And revenue financing is a type of equity financing;
> Therefore, revenue financing must have a higher cost of capital than debt.[172]

Revenue financing is not a type of equity financing. Unlike an investor-owned utility's equity financing, which aims to provide a certain return on investment for its investors, BPA does not have investors. Paying dividends or a rate of return to equity investors is not a cost that BPA incurs. There is no additional cost to BPA revenue financing—it is the exact same amount as the capital that it was used to invest in with no interest, rate of return, dividend, or otherwise, added on top. The overall cost of revenue financing is lower than the cost of debt financing with interest.

BPA disagrees that it should compare the cost of revenue financing against the opportunity costs of BPA's customers and their retail consumers. Instead, BPA considered the impact of revenue financing imposed on customers through increased rates. BPA is not borrowing from its customers, and its customers do not take on the role of investors. BPA's customers are not investing money in BPA to make a profit, and BPA is not aware of any utilities that routinely use long-term debt to pay for normal operating expenses such as their power and transmission service bills. They are paying a bill in exchange for a product or service. Compared to 100 percent debt financing, this policy may increase the near-term expense for those bills, but has a lower total cost—to be recovered through rates—over the course of a foregone bond. This is a long-term benefit to BPA and its customers in the form of lower costs over the long term, in addition to the other areas listed in Section 2.6.

Decision

Revenue financing does not have a higher cost of capital than debt financing.

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171 *Id.* at 6.
172 *Id*.

Issue 4.2.2.5

Whether inclusion of revenue financing in the Sustainable Capital Financing Policy raises governance concerns.

Public Comments

MSR argues that revenue financing is inconsistent with BPA's statutory standards,[173] and that BPA's decision to revenue finance, therefore, "raises serious market and governance questions."[174]

MSR claims that "market constraints will place a ceiling on the escalation of revenue requirements,"[175] and concludes "[t]he market is a viable constraint on [secondary power] sales; the market is a limited constraint on Preference customer [power] sales—particularly in the long-run; and the market provides no protection to transmission customers."[176] MSR states that "[w]here market constraints (*i.e.*, competition) are inadequate to protect electric customers, regulatory bodies have been created to simulate market constraints. Essentially, non-competitive situations become cost-based through regulatory oversight."[177]

MSR describes various oversight on BPA's decisions, including FERC limited review under Section 7(a)(2) of the Northwest Power Act, and "ultimately [review by] the courts if rate actions violate BPA's statutory requirements." MSR asserts that "BPA self-determines its obligation to set rates at 'the lowest possible rates to consumers consistent with sound business principles.'"[178] MSR contrasts BPA's "self-regulation" with investor-owned utilities and some publicly-owned utilities that "are subject to direct regulation of their rates and terms of service under the scrutiny of state regulatory commissions and consumer advocates[.]"[179] MSR also constrasts BPA with some publicly-owned utilities that "are regulated by their local governing body, an elected body, so customers, as voters, have a direct feedback loop into ratemaking decisions."[180]

MSR views the BP-22 rate case as a turning point: "Prior to the 2022 rate case, BPA reasonably adhered to the cost-based methodology for setting rates. . . . However, in the 2022 rate case, BPA formally included a non-cost-based line item of revenue financing."[181] MSR states that, although a settlement was reached for "a one-time inclusion of $40 million of revenue financing for each of the two business lines . . . [c]ritical to this settlement was the recognition that the revenue was one-time only and non-precedential."[182] MSR states that "[c]ustomers agreed to the one-time inclusion of revenue financing as a 'bridge' to a

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173 MSR Comments at 12.
174 *Id.* at 9.
175 *Id.*
176 *Id.* at 10.
177 *Id.*
178 *Id.* at 11.
179 *Id.* at 10-11.
180 *Id.*
181 *Id.* at 11.
182 *Id.*

more sustainable capital sourcing strategy," and that "M-S-R, along with many other customers, logically presumed that the subsequent increase in BPA's borrowing authority from $7.7 billion to $17.7 billion would alleviate the need for additional revenue financing in the setting of future revenue requirements."[183] MSR argues that revenue financing in this Policy "suggests that BPA has abandoned its commitment to cost-based rates," and will violate sound business principles by raising costs when Treasury borrowing authority is available.[184]

Evaluation

MSR acknowledges that statutory obligations exist, along with paths to review whether BPA's rates are consistent with those standards.[185] Nonetheless, MSR argues both that BPA's Policy violates those statutory standards, and that these violations raise "serious market and governance questions."[186] As discussed in Sections 4.2.2.1 and 4.2.2.2, the Sustainable Capital Financing Policy is consistent with BPA's statutes. BPA also disagrees that the adoption of this Policy raises governance concerns.

Foundationally, BPA sets its rates to recover its costs, consistent with statutory directives.[187] BPA has no profit motivation: all revenues are applied to cover BPA's costs. Revenue financing is not a departure from cost-based ratemaking, or incremental to BPA's costs. Revenue financing is a cost.[188] Revenue financing in BP-22 was also not a departure from past practice of cost-based ratemaking; BPA has included revenue financing several times before,[189] and FERC has approved BPA's rates in each instance.[190]

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[183] *Id.* at 11-12.
[184] *Id.* at 12.
[185] *Id.* at 11.
[186] *Id.* at 9.
[187] *See supra* Issue2.3.
[188] *See supra* Issue 4.2.2.1.
[189] *See, e.g.*, 1983 Wholesale Power and Transmission Rate Proposal, Administrator's ROD, WP-83-A-02, at 74-75 (Bonneville decides to revenue finance 5 percent of construction and conservation program); 1985 Wholesale Power and Transmission Rate Proposal, Administrator's ROD, WP-85-A-02, at 59-67 (Bonneville decides to revenue finance 7.5 percent of new construction and conservation plant in service to ensure a reasonable "investment service coverage"); 1987 Wholesale Power and Transmission Rate Proposal, Administrator's ROD, WP-87-A-02, at 41-47 (Bonneville decides to revenue finances $39.3 million in FY 1988 and $49.8 million in FY 1989); 1993 Wholesale Power and Transmission Rate Proposal, Administrator's ROD, WP-93-A-02, at 87-88 (Bonneville decides to revenue finance WNP-2 capital expenditures with a service life of 10 years or less); 1996 Wholesale Power and Transmission Rate Proposal, Administrator's ROD, WP-96-A-02, at 74-78 (Bonneville decides to revenue finance $22 million per year for WNP-2 investments and $15 million per year for transmission investments).
[190] *U.S. Dep't of Energy – Bonneville Power Admin.*, 32 FERC ¶ 61,014 (1985) (approving Bonneville's 1983 power and transmission rates); *U.S. Dep't of Energy – Bonneville Power Admin.*, 39 FERC ¶ 61,078, 61,207-08 (1987) (approving Bonneville's 1985 power and transmission rates and finding Bonneville's decision to include 7.5 percent of revenue financing for an investment service coverage was "appropriate"); *U.S. Dep't of Energy – Bonneville Power Admin.*, 54 FERC ¶ 61,235 (1991) (approving Bonneville's 1987 power and rates and investment service charge); *U.S. Dep't of Energy – Bonneville Power Admin.*, 67 FERC ¶ 61,351 (1994) (approving Bonneville's 1993 power and transmission rates); *U.S. Dep't of Energy – Bonneville Power Admin.*, 80 FERC ¶ 61,118 (1997) (approving Bonneville's 1996 power and transmission rates).

BPA's capital financing decisions can impact BPA's overall costs and when those costs are recovered in rates. BPA considers how these decisions may impact its competitiveness—both in the near and long term—as a factor to be balanced among others. Retaining customers assures a wider rate base from which to recover BPA's costs, which results in lower rates and makes BPA's cost recovery more certain. Here, BPA has considered the near-term rate impact, as well as the long-term benefits in managing BPA's debt portfolio such as reducing fixed costs and maintaining financial flexibility in the future.

MSR's comment that BPA statutory rate processes are inadequate to provide appropriate "oversight" is belied by the facts. BPA's decisions are subject to administrative and judicial review under various applicable standards.[191] BPA conducts a ratemaking process that is far more complex and inclusive than any publicly-owned utility the agency is aware of. These proceedings are conducted pursuant to Federal statutory rules, and then submitted to FERC for review and approval.[192] BPA's budget submittals are also subject to Congressional oversight.[193] Further, unlike investor-owned utilities, BPA does not pay dividends to shareholders, and therefore does not include—and does not require regulatory oversight to determine—a reasonable return on shareholders' investment as a cost to be recovered through its rates.

Regarding MSR's characterization of the BP-22 settlement, Parties did reserve their right to challenge future revenue financing decisions.[194] However, BPA did not agree to give up its ability to make capital financing decisions. Within BP-22 testimony, Staff made clear that revenue financing was not only to alleviate the impending borrowing authority crisis, but was also part of prudent debt management.[195]

In sum, BPA continues to set cost-based rates, including revenue financing as it has done on several prior occasions. BPA acts in accordance with the substantive statutory standards that apply to its ratemaking, and appropriate processes and oversight exists.

<u>Decision</u>

Inclusion of revenue financing in the Sustainable Capital Financing Policy does not raise governance concerns.

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191 *See e.g.,* Northwest Power Act § 7(a), 16 U.S.C. § 839e(a) (establishment; period review and revision; confirmation and approval by Federal Energy Regulatory Commission); Northwest Power Act § 9(e), 16 U.S.C. § 839f(e) (Judicial review; suits).
192 *See* Northwest Power Act § 7(i), 16 USC § 839e(i).
193 Transmission System Act § 11(a)-(b), (d), 16 U.S.C. § 838i(a)-(b), (d).
194 BP-22 Rate Proceeding, Administrator's Final ROD, BP-22-A-02, Appendix A at 3.
195 Fredrickson *et al.,* BP-22-E-BPA-36, at 40 ("[I]ncreased borrowing authority would do nothing to address BPA's concerns about relying on 100 percent debt financing or Transmission's growing debt outstanding issue.").

Issue 4.2.2.6

Whether BPA should focus on spending less instead of revenue financing.

<u>Public Comments</u>

MSR suggests, "BPA should focus on the avoidance of spending if it is concerned with the level of its debt."[196] MSR notes that the Leverage Policy included "reducing planned capital spending" as an action BPA could take to reduce a business unit's debt-to-asset ratio, and objects that this element does not appear in the Sustainable Capital Financing Policy.[197] MSR references BPA's Financial Plan Refresh presentations on capital investment prioritization,[198] capital framework,[199] and capital metrics,[200] but believes the action to spend less "does not appear to be honored in practice" as evidenced by "BPA's presentations on the Vancouver Control Center continu[ing] to favor the most capital intensive and expensive option."[201]

<u>Evaluation</u>

MSR is correct that the Sustainable Capital Financing Policy does not include capital spending reductions as an alternative to revenue financing. BPA, nonetheless, thinks critically about potential capital investments and cost control measures, even if they are not captured in this specific policy. Cost management discipline remains a Key Financial Objective in the draft Financial Plan.[202] BPA's capital planning and decisions to invest in specific projects are separate and distinct decisions from BPA's decisions regarding the form of financing used to fund such projects. The Sustainable Capital Financing Policy is focused on the latter.

In the public workshops, BPA gave an overview of its Asset Management Program and how it follows the framework of the Institute of Asset Management (IAM) and ISO 55000. A key part of BPA's Asset Management is implementing Criticality, Health and Risk (CHR) into its capital decision process to help ensure BPA is making the right capital decisions at the right time. In addition, BPA provided an overview of its project approval process for capital business cases, which is designed to help ensure that BPA selects the right alternative for each project to best meet the project objectives at the lowest lifecycle cost.

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196 MSR Comments at 14.
197 *Id.* at 13, n.11.
198 Bonneville Power Administration, *Financial Plan Refresh: Public Workshop* (Jan. 12, 2022), https://www.bpa.gov/-/media/Aep/finance/financial-plan-refresh/jan-12-final-workshop-presentation.pdf.
199 Bonneville Power Administration, *Financial Plan Refresh: Public Workshop* (Feb. 9, 2022), https://www.bpa.gov/-/media/Aep/finance/financial-plan-refresh/feb-9-capital-workshop-transmission-v3.pdf ("Feb. 9 Presentation").
200 Bonneville Power Administration, *Financial Plan Refresh: Public Workshop* (Mar. 9, 2022), https://www.bpa.gov/-/media/Aep/finance/financial-plan-refresh/20220309-public-presentation.pdf ("Mar. 9 Presentation").
201 MSR Comments at 13.
202 Bonneville Power Administration, *Draft Financial Plan*, 5 (May 2022), https://www.bpa.gov/-/media/Aep/finance/financial-plan-refresh/draft-financial-plan-2022.pdf.

In the February 9, 2022, workshop, BPA explained its capital prioritization process for seven asset categories and how CHR is used for each category. Potential investments are assessed and scored based on CHR, as well as professional judgement. For Transmission Services, 50-70 percent of capital spending is related to "sustain" work on existing assets, where the asset management process helps control costs. For the 30-50 percent of Transmission capital spending that is related to system expansion, the main drivers are in the important areas of safety, compliance, reliability, and customer requests.[203]

BPA provides customers with the opportunity to understand its near- and longer-term capital investment plan and strategy, as well as the chance to provide feedback on these plans, through its IPR process. Additionally, BPA provides a forum for regular updates on large projects during the technical Quarterly Business Reviews (QBR).

These processes assist BPA in making intelligent, targeted investments in support of its statutory mission without undue cost.

Decision

BPA is pursuing capital cost management outside of the Sustainable Capital Financing Policy.

4.2.3 Policy Goals

Issue 4.2.3.1

Whether achieving agency and business unit debt-to-asset ratios no greater than 60 percent by 2040 is a reasonable goal.

Public Comments

Snohomish "supports the goals, approach and flexibility embedded in the Draft Sustainable Capital Financing Policy," including BPA's "looking at the Draft Sustainable Capital Financing Policy as a means to achieve a 'more stable cost of service over time.'"[204]

Several commenters contend that the Policy's leverage goal is too aggressive.[205] NIPPC *et al.* state, "[t]his target may be inconsistent with establishing the lowest possible rates consistent with sound business principles."[206] These comments revolved around five main themes, which are summarized and evaluated in this order:

1. BPA did not compare itself to similar entities in determining its goal;
2. Achieving 60 percent leverage would have little credit rating impact;
3. Achieving the goal will require higher rates and little benefit to customers;
4. Achieving the goal could hamper BPA's ability to respond to industry change; and
5. Alternative proposals.

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203 Feb. 9 Presentation at 4.
204 Snohomish Comments at 1.
205 Av Avangrid *et al.* Comments at 5; AWEC Comments at 2; Central Lincoln Comments at 1; MSR Comments at 7-8; NIPPC *et al.* Comments at 1-4; NIPPC Comments at 1-5; OPUC and WUTC Comments at 1; PNGC Comments at 1; PPC Comments at 2; WPAG Comments at 1.
206 NIPPC *et al.* Comments at 1.

Comparable Entities

As discussed in Section 2.6, BPA considered industry practice in determining its leverage goal. Several commenters argue BPA looked to inapt comparators, and that BPA must be distinguished from investor-owned and publicly-owned utilities.[207]

NIPPC *et al.* have identified entities that it believes are more comparable to BPA, and that have higher leverage ratios.[208] MSR, PNGC, and Avangrid *et al.* generally concur.[209] WPAG states there are "a lack of entities comparable to BPA that have also adopted this aggressive metric."[210]

MSR argues that BPA's Treasury debt is fundamentally different than other forms of debt because the indexed Federal interest remains the same regardless of BPA's leverage, Treasury debt does not contain default provisions and risk of foreclosure, and has the characteristics of preferred stock.[211] Central Lincoln "believes similar entities with access to Treasury borrowing authority would likely have a higher leverage ratio as that debt should have more favorable terms and carries lower risk than non-Treasury debt."[212] PNGC argues the equity used by investor-owned utilities and publicly-owned utilities is different from BPA's revenue financing.[213]

Credit Rating Impact

NIPPC *et al.* argue that 60 percent leverage is not necessary because leverage is only one piece of an entity's financial health and credit rating agencies already believe BPA is healthy.[214] All else equal, remaining at 80 percent leverage would not result in a credit rating downgrade, and deleveraging to 60 percent would not result in a credit rating upgrade.[215]

NIPPC provided supplemental comments recommending that BPA "restudy its debt ratio calculation and provide a better description to better inform investors of actual leverage when compared to other utilities."[216] NIPPC asserts that "BPA is already at a 60 percent debt ratio if US Treasury line is considered."[217]

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207 NIPPC *et al.* Comments at 2-3; MSR Comments at 7; PNGC Comments at 1; NIPPC Comments at 1; Central Lincoln Comments at 1; NRU Comments at 1; Avangrid *et al.* Comments at 5.
208 NIPPC *et al.* Comments at 2-3 (citing NIPPC, *Bonneville's Financial Plan Refresh and its Credit Ratings* (Dec. 20, 2021), https://www.bpa.gov/-/media/Aep/finance/financial-plan-refresh/nippc-paper-20-december-with-disclaimer.pdf); NIPPC Comments at 2-4.
209 MSR Comments at 7; PNGC Comments at 1; Avangrid *et al.* Comments at 5.
210 WPAG Comments at 1.
211 MSR at 7-8.
212 Central Lincoln at 1.
213 PNGC Comments at 1.
214 NIPPC *et al.* Comments at 2.
215 *Id.*
216 NIPPC Comments at 3.
217 *Id.*

Benefit to Customers

Central Lincoln believes that BPA's current leverage ratio is appropriate, and that the "60% target is likely to lead to higher rates than necessary for preference customers, due to the need to revenue finance to achieve it."[218] AWEC "is concerned that BPA's targeted leverage ratio remains unnecessarily aggressive without a clear indication of the benefits to customers."[219] NIPPC *et al.* argue that deleveraging to 60 percent "is unlikely to provide any material benefit to customers, but it will cost customers approximately $1.6 billion in net revenue financing."[220] NIPPC *et al.* suggest that "BPA customers could invest that $1.6 billion in any number of other ventures, including financing new clean energy projects, reducing electric bills for their own customers, building new transmission lines, or hardening the grid against wildfires and other extreme weather."[221]

Ability to Respond to Industry Change

WPAG cautions that "[t]here are many things that will change during the run-up to 2040 and too aggressive of an initial goal can have unintended consequences."[222]

OPUC and WUTC state that Oregon and Washington "investor-owned utilities and their customers and suppliers depend on BPA's transmission activities to meet their reliability and clean energy needs at a critical juncture for the West."[223] "The region needs BPA to be a leader in delivering a transmission system that serves the entire region, and we are concerned that by adopting a conservative long-term financial target for the transmission business unit, BPA is signaling that it does not prioritize that leadership role."[224]

NIPPC *et al.* state this policy "is being proposed precisely when BPA's extraordinary plenary authority to construct transmission is most needed to meet the region's—and the Biden Administration's—energy goals."[225]

Alternative Proposals

Several commenters proposed alternate goals, as discussed in more detail below. NIPPC *et al.* propose a 70 percent target by 2040, with planned reconsideration in 2026, and an interim trigger for higher revenue financing.[226] AWEC proposes a debt-to-asset ratio of 70-80 percent.[227] WPAG proposes a higher target, and agrees with NIPPC that 70 or 80 percent could be as effective.[228] PPC has concerns with the 60 percent target and would support either the NIPPC proposal or BPA maintaining openness to new information in

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218 Central Lincoln Comments at 1.
219 AWEC Comments at 2.
220 NIPPC *et al.* Comments at 2.
221 *Id.*
222 WPAG Comments at 1.
223 OPUC and WUTC Comments at 1.
224 *Id.*
225 NIPPC *et al.* Comments at 3.
226 *Id.* at 3-4.
227 AWEC Comments at 2.
228 WPAG Comments at 2.

several rate periods.[229] NIPPC's supplemental comments recommend a 70 percent target with a "circuit breaker."[230]

Evaluation

As discussed in Issue 4.2.2, revenue financing is an appropriate financing tool with long-term benefits. While MSR argues that 100 percent debt financing and 100 percent leverage may be appropriate,[231] and AWEC recommends BPA "decline to move forward with revenue financing as part of the Financial Plan Refresh at this time,"[232] commenters generally appear to recognize that revenue financing may be appropriate under certain conditions, and that moving away from 100 percent debt financing is an appropriate goal. For example, WPAG states, "Bonneville has made a compelling case that continuing to debt finance 100 percent of the capital program is unsustainable," but describes the 60 percent target as "aggressive."[233] NIPPC *et al.* state:

> We agree with a premise that there is an upper limit of debt that an entity like BPA can prudently bear. We are not arguing here for BPA to eliminate a debt utilization policy nor to adopt a significantly higher target, for example, a 100% debt ratio. Instead, the gap between BPA's proposal and what we propose is a matter of degrees.[234]

Arguments in this section go to whether the degree of revenue financing—*i.e.,* in amounts intended to achieve 60 percent leverage by 2040—is permissible and reasonable.

BPA's goal is reasonable, as confirmed by comparisons to similar, but distinct, entities

Foundationally, BPA did not determine its goal of achieving 60 percent leverage by 2040 by identifying a pool of the most accurate comparators and calculating the median value. Instead, BPA recognizes there are competing considerations to be balanced in making financing decisions. The purpose of surveying industry practice was to confirm that our goal was reasonable and grounded in industry practice. Our initial survey was supplemented by considering the additional analysis and comparators provided by commenters. These comparisons confirmed BPA's goal.

After comparing and contrasting itself with similar, yet distinct, entities, BPA Staff characterized the Policy goal as "at the upper end[235] of the spectrum for what is considered financially healthy for leverage goals, and [taking] a long-term approach to achieving this goal."[236] Commenters have considered the same data and characterize BPA's goal as

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[229] PPC Comments at 2.
[230] NIPPC Comments at 3.
[231] MSR Comments at 8.
[232] AWEC Comments at 2.
[233] WPAG at 1.
[234] NIPPC *et al.* Comments at 3.
[235] I.e., the least aggressive end.
[236] Comment Response Compilation at 32.

"aggressive,"[237] or presented proposals they believe are "more measured."[238] While BPA emphasizes different points when comparing and contrasting to other entities, the agency's goal is well within its expansive mandate to operate as a business and to take such actions as will ensure that BPA meets its various statutory obligations.[239]

Several commenters take issue with BPA's initial industry survey, and argue that BPA should not have compared itself to investor-owned utilities or publicly-owned utilities.[240] MSR asserts that investor-owned utilities and publicly-owned utilities "are so different from BPA that the comparison provides no value."[241] In distinguishing BPA, NIPPC *et al.* note BPA is not a "capital-constrained utility with a very limited pool of ratepayers and no sovereign backing from the U.S. government."[242] PNGC separately adds that BPA is "a Federal agency with its own ratemaking authority, long-term contracts and unique borrowing authority."[243]

BPA recognizes that it has characteristics that are similar to, and different from, other entities, and therefore any comparison will be imperfect. BPA has generation and transmission, as do many entities BPA compared to. Like other public entities, BPA sets rates to recover its costs. BPA operates within the U.S. in the same markets as many of the identified utilities. BPA therefore faces some of the same inherent market and environmental risks as the entities it compared to. BPA is, however, a Federal entity, which many comparators are not, and has a financing arrangement with the U.S. Treasury to borrow money, although it is paid back with interest like commercial debt. Even with these similarities and differences, these utilities remain relevant as points of reference in confirming that BPA's goal is reasonable and grounded in industry practice. Because the comparisons are imperfect, reasonable minds will disagree on what implications should be drawn from the comparison. Further, even if an entity existed with BPA's exact attributes, BPA would not be required to adopt their current leverage ratio as its target. An entity's leverage ratio is the result of business-minded decisions that balance short- and long-term objectives. This Policy seeks to balance those objectives through a long-term policy that sustainably guides our capital financing decisions.

While BPA is not identical to any specific public utility, or even to other power marketing administrations or the Tennessee Valley Authority (TVA), ratings agencies believe certain categories are useful points of comparison. BPA recognizes that is has credit-positive attributes that are not shared by all entities in these categories. Nonetheless, independent credit ratings agencies include BPA in certain categories because they believe, BPA has characteristics that are comparable to the other entities in the categories. Fitch includes BPA in its *Public Power-Peer Review* reports. Moody's includes BPA in its *Public Power*

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[237] WPAG Comments at 2.
[238] NIPPC *et al.* Comments at 4.
[239] *See Ass'n of Pub. Agency Customers, Inc.*, 126 F.3d at 1171.
[240] NIPPC *et al.* Comments at 2-3; MSR Comments at 7; PNGC Comments at 1; NIPPC Comments at 1; Central Lincoln Comments at 1; NRU Comments at 1; Avangrid *et al.* Comments at 5.
[241] MSR Comments at 7.
[242] NIPPC *et al.* Comments at 3.
[243] PNGC Comments at 1.

Sector-in-Depth reports. Whether considering all rated public utilities, including TVA, wholesale and generation and transmission cooperatives, wholesale only, or all rated Pacific Northwest utilities, BPA is an outlier.[244] The debt management practices and lower leverage of these utilities are evidence that BPA's long-term goal is reasonable. Further, although these utilities often have leverage ratios in the 40-60 percent range, BPA's goal targets the upper end of this range, and BPA does not expect to achieve that goal until 2040. That is, BPA expects its leverage to be greater than 60 percent over the next two decades.

In disagreeing with BPA's initial survey, MSR lists differences between BPA and investor-owned or publicy-owned utilities including "(1) the interest rate relationship to debt-to-asset ratios; (2) obligations to make principal and interest payments; (3) governance; and (4) different assets and functions."[245] While these are differences, publicly-owned utilities remain relevant comparators for BPA. First, if there is a relationship between interest rates and an entity's debt-to-asset ratio, BPA's non-Federal debt—which constitutes about half of its portfolio—is exposed to that risk. Second, BPA has statutory obligations to ensure the repayment of principal and interest, which as discussed below, may be more strict than other utilities. Third, as discussed in Issue 4.2.2.5, BPA's governance structure is different but not without constraint. Fourth, as for assets and functions, all of BPA's customers, whether utilities or marketers, are different. Some have only distribution facilities. Some also have generation and transmission facilities. Some have no facilities and purely market power. Regardless of the assets and functions, it is clear that public entities with capital assets and construction programs generally do not rely on 100 percent debt financing. They rely on revenues collected through rates, and often to a far greater degree than BPA is proposing.

Several commenters argue BPA should compare itself against different entities than those in BPA's initial survey.[246] Throughout the process, commenters have identified entities that they believe are more comparable to BPA, and that have higher leverage ratios than BPA's long-term goal. BPA has considered these additional comparators, noting important distinctions between BPA and these entities and—to the extent these entities are comparable—discussing how the comparison supports BPA deleveraging.[247] These additional comparators confirm that BPA's goal is reasonable and grounded in industry practice.

NIPPC's presentation at the January 26, 2022, workshop suggested BPA compare itself against Fingrid Oyj, Hydro-Quebéc, Statnett, and the TVA.[248] Staff noted that the first three

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[244] *Supra* Section 2.6.
[245] *Id.*
[246] NIPPC *et al.* Comments at 2-3; MSR Comments at 7; PNGC Comments at 1; Avangrid *et al.* Comments at 5; WPAG Comments at 1; Central Lincoln Comments at 1.
[247] Comment Response Compilation at 31-33, 58-61.
[248] NIPPC Presentation at 5.

are entirely majority owned by foreign governments, and appear to be regulated like an investor-owned utility in the United States.[249] "Unlike BPA," Staff noted:

> [A]ll three pay significant dividends to their owners, which provides an incentive to maximize borrowing. The government owners are able to adjust the dividend paid by the utility to meet the financial needs of the utility or the government. The Norwegian government, for example, cut the dividend from Statnett in half in 2014-18 when the utility had ramped up its construction program, which appears as if the government was allowing the utility to use revenues to support the capital spending.[250]

Staff further explained that these three utilities as comparators supported BPA's deleveraging goal:

> Although other credit positives may compensate for BPA and these European entities' poor leverage position and prevent a downgrade, none of the reports suggest that an 80% leverage is a good thing. Fingrid demonstrates that new builds for renewable development, with a heavy reliance on debt, can strain financial metrics, which supports BPA taking steps to maintain financial flexibility. Hydro-Quebec has lower leverage than BPA(around 70%), even with much stronger government support than BPA. Moody's and S&P set Statnett's 80% leverage at the stand-alone equivalent of Baa2 and BBB levels.[251]

As for TVA, BPA Staff recognized a similarity in that neither BPA nor TVA pay a dividend to the Federal government.[252] Staff also noted that TVA's debt-to-asset ratio was 61 percent as of FY 2020.[253] This ratio follows TVA's recent dramatic increase in debt repayment to improve its balance sheet, including TVA's ability to include in its rates "such additional margin as the TVA Board may consider desirable for investment in power system assets."[254] Considering these additional utilities also confirms that BPA's goal is reasonable and grounded in industry practice.

In comments following the February 23, 2022, workshop, Renewables Northwest and NRDC suggested BPA evaluate its goals compared to the industry average for Federally-supported public entities similar to BPA.[255] In response, BPA Staff considered the three other power marketing administrations—the Western Area Power Administration (WAPA), the Southwestern Power Administration (SWPA), and the Smart Electric Power Alliance (SEPA)—and TVA.[256] Staff stated:

> It is difficult to perfectly compare leverage calculations to Bonneville because of differences in how data is reported. However, all four agencies do make

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249 Comment Response Compilation at 31-33.
250 *Id.* at 31-32.
251 *Id.* at 32.
252 *Id.*
253 *Id.* at 32, 41.
254 *Id.* at 32.
255 *Id.* at 41.
256 *Id.*

> available annual financial data, either through in annual report or a 10-K filing with the SEC. By our calculation, TVA's ratio was about 61% as of FY 2020. The ratios for WAPA, SWPA, and SEPA may not be comparable without additional detail because their annual reports show "payable to U.S. Treasury," which include more than just the repayment of debt associated with capital investment. For example, this category includes interest owed to the Treasury. The PMAs receive appropriations for all of their costs, which must be repaid from revenues, so they may consider all costs payable to the Treasury. If we were to assume that SWPA and SEPA were only reporting payables associated with debt repayment—which does not appear to be the case—their ratios would be 100% and 129% respectively. WAPA, which has other long-term liabilities unlike SWPA and SEPA, had a leverage ratio [that] was about 49% as of FY 2020. If we were to combine the data for the three PMAs and TVA, the combined leverage ratio would be about 64%.[257]

While differences make a direct comparison difficult, considering these additional utilities also confirms that BPA's goal is reasonable and grounded in industry practice.

NIPPC proposed additional comparators, along with brief justifications, in comments following the March 23, 2022, workshop. NIPPC identified the Transmission Agency of Northern California (TANC), Sacramento Municipal Utility District (SMUD), and the Joint Action Agency (JAA) sector as "public power utilities that do have high debt-to-asset ratios," but acknowledged, "it is also clear these or other utilities do not have BPA's value and dominance in their region due to fundamental factors such as competitiveness, environmental stewardship, clean generation asset value, and financial record."[258] NIPPC's representative clarified that the JAA sector is not "a better sector to compare to, only that the concept of leverage needs more work as it related to BPA."[259] NIPPC distinguished BPA from TVA, and suggested additional international comparators.[260] NIPPC identified certain utilities that it believes are not good comparators: the New York Power Authority, Lower Colorado River Authority, Grand River Dam Authority, and Missouri River Energy Services, "who have lower ratios . . . [but] generation assets **substantially** less than BPA, do not have the same level of parent support, and have limited transmission assets (except for NYPA)."[261] As NIPPC's analysis recognizes, these additional entities have some similarities as well as important differences. Considering these examples does not show BPA's goal is unreasonable.

In its most recent supplemental comments, NIPPC proposed additional comparators, including the Top 7 U.S. Generation and Transmission (G&T) Cooperatives, the JAA sector, Lower Colorado River Authority (LCRA), Santee Cooper, andLong Island Power

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[257] *Id*. at 41-42.
[258] NIPPC Apr. 6 Comments, Appendix 1 at 3.
[259] NIPPC Apr. 6 Comments at 5.
[260] *Id.* at 3-4 ("I would add others, for example, Manitoba Hydro, which has a debt to capitalization ratio averaging 87% over the past 5 years and BC Hydro debt ratio exceeded 80% in 2021-2022.")
[261] *Id.* at 5

Authority.[262] BPA considered these comparators and determined the comparison supports BPA's policy goal. BPA had previously included Wholesale and G&T Cooperatives within its industry survey.[263] NIPPC's prior comments explained why the JAA sector and LCRA were inapt comparators, and BPA further notes the LCRA Board's financial policy specifically states that revenues will be used to fund capital projects.[264] In the case of Santee Cooper, it was not targeting a specific debt to asset ratio. Instead, as NIPPC notes, its debt recently doubled as a result of terminating construction of unfinished nuclear plants leaving it with no asset to match.[265] Still, Santee Cooper, like other utilities, uses "internally generated funds" to finance capital projects and is retiring existing debt faster than it issues new debt, reducing its outstanding debt by $1.4 billion between 2016-2020.[266] That is, Santee Cooper uses revenues from rates to finance part of its capital program and has become a net debt repayer. In addition, while Long Island Power Authority's (LIPA) debt-to-asset ratio was 97.5 percent in 2020, it recently adopted specific actions "intended to continue to reduce the Authority's debt-to-assets ratio to a level of roughly 70% by 2028."[267] Therefore, LIPA's goal is to deleverage 27.5 percent over the course of eight years. This is far more aggressive than BPA's goal, which has each business unit deleveraging by the same percentage or less, but over an 18-year period, rather than the eight-year period adopted by LIPA.

BPA agrees that the additional entities identified throughout the Financial Plan Refresh process, including those proposed by NIPPC, are relevant for BPA to consider. Having considered the examples of these entities, and the ways in which they are similar and distinct from BPA, BPA finds that the comparisons confirm BPA's goal is reasonable and grounded in industry practice. The comparators do not require a certain result for BPA. This policy process is not an effort for BPA to emulate any single utility, and the existence of entities with leverage ratios currently higher than where BPA hopes to be in 20 years does not necessarily mean BPA should emulate them. Some utilities discussed have leverage ratios higher than BPA's, just as others have ratios far lower. Each of the utilities suggested by commenters faces unique circumstances, but notably none of these utilities 100 percent debt finances their capital program. There are no identical comparators, and BPA and commenters may disagree on the implications to be drawn from various

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262 NIPPC Comments at 2-4.
263 *See supra* Section 2.6.
264 Lower Colorado River Authority, Board Policy 301 Finance, § 301.303 (Dec. 14, 2021), *available at* https://www.lcra.org/download/301-pdf/?wpdmdl=17930.
265 S&P Global Ratings, South Carolina Public Service Authority, May 6, 2022 at 5, *available at* https://www.santeecooper.com/About/Investors/_pdfs/Credit-Rating/SP-Rating-report-May-06,-2022.PDF.
266 Santee Cooper, *About the Debt of Santee Cooper* (last visited July 14, 2022), https://www.santeecooper.com/About/Increasing-Value/Progress-Reports/_pdfs/About-the-Debt-of-Santee-Cooper-20210128.pdf.
267 Long Island Power Authority, *Summary of the 2020 Financial Policy Report*, 5 (Nov. 18, 2020), https://www.lipower.org/wp-content/uploads/2021/03/2020-Financial-Policy-Report.pdf; Long Island Power Authority, *Annual Disclosure Report Supplement*, 7 (June 29, 2021), https://www.lipower.org/wp-content/uploads/2021/06/Annual-Continuing-Disclosure-Report-including-financials-for-the-Fiscal-Year-2020-1.pdf.

comparisons. However, BPA views these entities as providing additional evidence that BPA's goal is reasonable and grounded in industry practice.

As a separate matter, MSR and Central Lincoln argue that BPA's Treasury borrowing is different than other forms of debt, and therefore could support a higher leverage ratio.[268] More specifically, MSR argues BPA's Treasury debt is fundamentally different because (1) the indexed Federal interest remains the same regardless of BPA's leverage, (2) it does not contain default provisions and risk of foreclosure, and (3) it has the characteristics of preferred stock.[269]

But the fact that Treasury debt is different does not mean that a higher leverage ratio is acceptable, or that it is without cost. Unlike utilities with access to the commercial markets, BPA has a fixed and finite amount of debt that it can issue to the U.S. Treasury. Utilities with access to commercial markets do not have a statutory limit on the amount of debt that they can issue. Instead, the key limiter is likely to be what their boards consider acceptable costs and the interest rates demanded by lenders and what the market will lend based upon their credit profile. Still, BPA's Treasury borrowing is not without risk. A deferral of principal or interest payments can force up interest rates on BPA's debt, and the deferred payments must be repaid before any other. Deferral also creates considerable political risk for BPA. The last BPA deferrals in the late 1970s and early 1980s led to multiple attempts to dismantle the agency. As for the comparison to preferred stock, the relationship between BPA and the U.S. Treasury is that of a borrower and lender, not corporation and stockholder.

PNGC argues that, although "PNGC is not fundamentally opposed to the concept of revenue financing[,] . . . the equity used by IOUs and even COUs is owned by IOU shareholders or in the case of COUs by customers or members of those utilities. BPA is not providing a similar result here. BPA should not 'extract' equity from customers this way."[270] We understand this argument to be that BPA should not compare itself to the leverage ratios of IOUs and COUs, because their equity financing is different than BPA's. First, BPA's comparisons have not been to IOUs. IOUs finance their capital programs with a mix of debt and equity. IOU rates include a return on equity financing to pay dividends to shareholder investors. BPA's revenue financing is not equity financing. There is no dividend earned on the revenue financing. Further, a public utility district with revenue financing does not pay a dividend to its customers. For BPA, revenue financing is one component of financing a portfolio of assets. While there is no dividend associated with revenue financing, there is an overall net benefit because there is no associated interest payment.[271] BPA is not "extracting equity from customers;" revenue financing is a different tool than equity financing.

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[268] MSR Comments at 7-8; Central Lincoln Comments at 1.
[269] MSR Comments at 7.
[270] PNGC Comments at 1.
[271] *See* Issue 4.2.2.1.

Achieving 60 Percent Leverage Would Be Viewed as a Credit Positive

NIPPC *et al.* review Moody's scorecard and Fitch's methodology to conclude that, all else equal, remaining at 80 percent leverage would not result in a credit rating downgrade, and deleveraging to 60 percent would not result in a credit rating upgrade.[272] Fitch's methodology weighs leverage against two other factors—revenue defensibility and operating risk.[273] NIPPC *et al.* argue that, "[s]o long as the other two factors hold true, it makes no difference to Fitch's rating whether BPA debt ratio is 60%, 70%, or 80%."[274] Moody's scorecard associates leverage between 60 percent and 80 percent with an 'A' rating, and leverage between 35 percent and 60 percent with an 'Aa' rating.[275]

BPA has been clear that, consistent with the Financial Plan, its objective is to maintain high investment-grade ratings, not to improve BPA's rating. While credit ratings impact the cost of debt, BPA also values that credit rating agencies provide an independent assessment of the agency's financial health. However, in our most recent rating, Moody's stated that "BPA's rating is likely to be upgraded if BPA maintains or expands its credit supportive goals and policies under its new financial plan, while having access to the larger borrowing line."[276] The Sustainable Capital Financing Policy is not designed to achieve a credit rating upgrade. However, achieving 60 percent leverage would be viewed as a credit positive and indicator of financial strength, among many other benefits.

NIPPC *et al.* state, "Fitch has indicated a tolerance for the ratio trending slightly higher . . . because transmission assets can support higher leverage than generation assets."[277] BPA expects Transmission will have a higher leverage ratio than Power even with the Sustainable Capital Financing Policy. By 2040, Power's leverage will approach 50 percent as Transmission approaches 60 percent.[278]

NIPPC provided supplemental comments asserting that "BPA is already at a 60% debt ratio if US Treasury line is considered."[279] NIPPC recommends BPA "restudy its debt ratio calculation and provide a better description to better inform investors of actual leverage when compared to other utilities."[280]

BPA disagrees that additional analysis on BPA's debt ratio is necessary to support the adoption of this Policy. Regarding the U.S. Treasury line of credit, it is important to note that the line of credit is part of BPA's Treasury borrowing authority. In other words, if used it results in debt. If the line of credit is treated as an asset, as NIPPC appears to be proposing, it must also be included as debt because the asset can only exist if the debt is issued. Correcting for this assumption eliminates any potential leverage reduction. As for informing investors, each of the credit rating agencies use their own permutation of a debt-

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272 NIPPC *et al.* Comments at 2.
273 *Id.*
274 *Id.*
275 NIPPC *et al.* Comments at 2.
276 Moody's Investor Service, *Credit Opinion: Bonneville Power Administration,* 3 (Apr. 6, 2022), www.bpa.gov/-/media/Aep/finance/rating-agency-reports/moodysfullreportmay2022.pdf.
277 *Id.*
278 Jan. 26 Presentation at 21, 25.
279 *Id.*
280 NIPPC Comments at 3.

to-asset ratio, regardless of the metrics used by individual entities for their own analytical purposes. Even if BPA revised how it calculates its ratio, it is far more likely that investors would consider the bond rating reports by Moody's, Fitch, and Standard & Poor's.

While BPA expects reducing leverage to be viewed as a credit positive and indicator of financial strength, the Sustainable Capital Financing Policy was not designed to achieve a credit rating upgrade. Instead, the Policy was designed to guide BPA's use of debt and revenue financing to finance its capital investments in order to manage BPA's outstanding debt, control its growth in relation to the value of the underlying Federal assets, and help to ensure a more consistent cost of service over time.

BPA Considered the Potential Near-term Rate Impact in Achieving Long-term Benefit

AWEC, Central Lincoln, and NIPPC *et al.* argue that achieving the leverage ratio goal will raise costs and rates without a clear benefit to customers.[281]

BPA recognizes that revenue financing—as compared to compared to debt financing—increases near-term costs to achieve long-term savings and other benefits. Within a portfolio context, capital financing decisions consider how much to pay now, and how much to pay later with interest. BPA developed this Policy with strong consideration for near-term rate impacts.[282] The Policy is designed to make progress towards its long-term goal over a 20-year horizon, with no greater than about 1 percent incremental rate impact per rate period. In BP-24, the expected default amount of revenue financing for Transmission is about the same as what would be required to meet the near-term target of the Leverage Policy. Holding Transmission's leverage flat, consistent with the Leverage Policy, would require $56 million of revenue financing, compared to the expected default amount of $55 million. The Policy also allows revenue financing to be repurposed for liquidity, which may prevent rate increases due to risk adjustment mechanisms like the Financial Reserves Policy (FRP) Surcharge and Cost Recovery Adjustment Clause (CRAC), and provides flexibility to respond to various circumstances. In these ways, the Policy balanced the near-term rate impact, while still allowing BPA and its customers to achieve the long-term benefits of revenue financing. Indeed, other comments support the Policy's goals "as a means to achieve a 'more stable cost of service over time.'"[283] And, as discussed in Issue 4.2.2.1, revenue financing results in an overall net benefit.

NIPPC *et al.* calculate a net cost of $1.6 billion to "deleverage an agency that does not remotely appear to be in danger of a credit rating downgrade or of default on its outstanding debt," and argues that customers could instead fund "any number of other ventures, including financing new clean energy projects, reducing electric bills for their own customers, building new transmission lines, or hardening the grid against wildfires and other extreme weather."[284] While NIPPC notes that BPA is not in danger of a credit rating downgrade or default on its outstanding debt, it is prudent to make incremental steps towards preventing such scenarios from occurring, instead of waiting for a crisis to

[281] AWEC Comments at 2; Central Lincoln Comments at 1; NIPPC *et al.* Comments at 2.
[282] *See infra* Issue 4.2.4.1.
[283] Snohomish Comments at 1.
[284] NIPPC *et al.* Comments at 2.

occur. We also note that, while customers' bills from BPA will be an expense, several of NIPPC's investment proposals would involve capital, which would likely be financed by BPA's customers with a combination of debt and equity or revenue financing.

BPA Can Respond to Industry Change and Achieve its Policy Goals

WPAG, NIPPC *et al.*, and OPUC and WUTC question BPA adopting a policy to achieve 60 percent leverage by 2040 during a time of change in the industry.[285]

BPA plays a pivotal role and is fully engaged in the changes occurring within our industry. BPA does not expect this Policy to impede infrastructure development or decarbonization efforts. Decisions about infrastructure investment are not driven by capital financing decisions. The Policy does not limit capital investment decisions, and the Policy expressly calls out "changes in BPA's capital program" as a circumstance that may warrant deviating from the Policy's default amount of revenue financing.[286] BPA' goal is not overly ambitious, achieving long-term benefits with no greater than 1 percent incremental rate impact per rate period.

Moreover, taking proactive steps now to maintain BPA's financial strength and flexibility will enable BPA to be able to respond to the volatility of an uncertain future. It is prudent to take a more conservative approach on debt in a utility business environment that has and is likely to continue to change rapidly. Continuing to nearly 100 percent debt finance BPA's capital program—and allowing Transmission to continue borrowing $2 billion per decade more than it repays, largely to maintain existing assets—adds an inflexible fixed cost to BPA's cost of service. Reducing leverage also reduces BPA's exposure to a changing interest rate environment. This Policy sets parameters that provide more certainty to customers, rather than make financing decisions on a rate-case by rate-case basis.

Alternative Proposals

NIPPC *et al.* propose an alternative policy with the following terms:

- A 70 percent debt ratio target for each business unit by 2040, with associated revenue financing to reach this target.
- Planned reconsideration of this 70 percent target in four years (2026), including evaluation of whether adopting a 60 percent alternative long-term target would be more financially sound.
- In the interim four years, a trigger: a significant spike (such as 300 basis points relative to today) in the Agency Rate charged by Treasury, to be evaluated annually. This trigger would shift BPA toward a lower debt-to-asset ratio and thus higher revenue financing in the subsequent rate period. This shift would be subject to the same constraints (approximately 1 percent incremental rate pressure from rate period to rate period)

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[285] WPAG Comments at 1; NIPPC *et al.* Comments at 2-3; OPUC and WUTC Comments at 1.
[286] Attachment 1, Sustainable Capital Financing Policy § 5.

proposed in the Draft Plan (p. 2 of the Draft Sustainable Capital Financing Policy).[287]

NIPPC *et al.* describe "the gap between BPA's proposal and what we propose [as] a matter of degrees."[288] NIPPC *et al.* "agree with a premise that there is an upper limit of debt that an entity like BPA can prudently bear" and "are not arguing here for BPA to eliminate a debt utilization policy nor to adopt a significantly higher target, for example, a 100% debt ratio."[289]

WPAG proposes "Bonneville should consider a higher and more realistic target" and stated, "NIPPC and others presented a compelling case that 70% or 80% goal would be just as effective."[290] PPC states it "continues to have concerns regarding the long-term goal of 60% leverage for the agency [and] would support the NIPPC proposal to begin with a target for 70% with a defined check in to see if moving to a more aggressive value is appropriate."[291] "Alternately," PPC proposes, "in several rate periods as circumstances change, we encourage BPA to maintain openness to new information on appropriate long-term leverage targets."[292]

NIPPC's supplemental comments recommend including "a 70% debt ratio target with a circuit breaker that prompts management to suspend progress towards [the] target should certain financial metrics weaken."[293]

AWEC proposes that, "should BPA continue to find that some level of revenue financing is appropriate, AWEC recommends it be at a level associated with a debt-to-asset ratio of 70-80 percent, subject to additional changes described [in its comments]."[294]

BPA appreciates commenters developing these alternative proposals, and thinking holistically through optionality. BPA appreciated the flexibility in NIPPC *et al.*'s "trigger" proposal, which would allow revenue financing—in certain conditions—to lower BPA's exposure to a volatile interest rate environment and achieve the benefit of avoided interest expense. However, the requirement that the increased revenue financing have the same incremental rate impact constraints would require the timeline to achieve 60 percent leverage to be extended further than 2040. BPA believes our Policy more reasonably guides capital funding decisions to balance the near-term impact and long-term benefits.

NIPPC *et al.* also propose starting with a lower target and revisiting the decision in four years. BPA agrees there is merit in periodically reviewing the Policy to ensure the Policy is operating effectively and continues to align with BPA's strategic direction. While BPA will

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287 NIPPC *et al.* Comments at 3-4.
288 *Id.* at 3.
289 *Id.*
290 WPAG Comments at 1.
291 PPC Comments at 2.
292 *Id.*
293 NIPPC Comments at 3.
294 AWEC Comments at 2.

retain its current target, the agency will agree to periodically review this Policy, as discussed in Issue 4.2.5.2.

BPA considered these alternative proposals, but believes its Policy goal will achieve greater benefits while reasonably managing near-term rate impacts. NIPPC *et al.* recommend their policy as "a more measured but still financially sound approach to the long-term debt ratio" that "remains in the range of the long-term goal (60-70%) in the current Leverage Policy."[295] Further, "it is anchored . . . at the mid-point of Moody's scorecard criterion for debt ratios . . . for an 'A' score, leaving a healthy margin for future adjustments (up or down) in BPA debt."[296] Their proposal "still moves BPA away from 100% debt financing by revenue financing approximately 5% of the annual capital spending" and "leaves the door open to incrementally increas[e] the amount of revenue financing in the future . . . ."[297]

This explanation, however, does not recognize the long-term nature of BPA's policy. Under NIPPC *et al.*'s proposal, BPA would not be "anchored at the mid-point" referenced by NIPPC for another two decades. Even under BPA's policy, the agency does not expect Transmission to reach 70 percent leverage for nearly a decade.[298] As for the Leverage Policy's long-term goal, although BPA will sunset the Leverage Policy, BPA notes that it does not expect to enter the range of the Leverage Policy's long-term goal for another decade under the Sustainable Capital Financing Policy; NIPPC *et al.*'s proposal would not have BPA enter that range until 2040. Regardless whether commenters believe 60 percent leverage is aggressive or measured, BPA's policy is designed to take a long time to get there.

Most importantly, a 70 percent leverage target will not achieve the same long-term benefits as a 60 percent target. Arguments that a higher leverage target would be "just as effective" focus only on whether BPA would maintain its current credit rating score and move away from 100 percent debt financing. The Sustainable Capital Financing Policy was designed to achieve additional long-term benefits and objectives.

As discussed in Section 2.6, BPA recognized that nearly 100 percent debt financing its capital program was unsustainable, and that there were long-term benefits to revenue financing. These long-term benefits needed to be balanced against the near-term rate impact and intergenerational equity considerations associated with revenue financing. Our Policy is designed to set parameters around capital financing decisions to reasonably balance these considerations. The 5 percent revenue financing expected to occur under NIPPC *et al.*'s proposal is significantly less than the common industry practice of rate financing 40-50 percent.[299] The 10-20 percent expected under BPA's Policy remains a modest step away from 100 percent debt financing. While achieving a 70 percent leverage

295 NIPPC *et al.* Comments at 4.
296 *Id*.
297 *Id.*
298 Jan. 29 Presentation at 25.
299 Oct. 19 Presentation at 20.

target by 2040 would have a smaller near-term rate impact, BPA disagrees that it appropriately balances this with the long-term benefits of revenue financing.

BPA performed additional analysis on alternative leverage goals,[300] but NIPPC *et al.* object to BPA's prior statement that a goal to achieve 70 percent leverage by 2040 "does not appreciably curb the growth in Transmission's debt outstanding and puts at risk our ability to provide a consistent cost of service over the long term."[301] They argue that "[t]his statement asserts the existence of a significant financial risk without providing any supporting basis" and that "[i]f gross debt, rather than the debt-to-asset ratio, is BPA's primary concern, then the Draft Plan should be redrafted on that basis."[302]

Throughout this process, BPA's analysis has considered factors beyond debt-to-asset ratio. BPA's additional analysis on achieving a 70 percent leverage target by 2040 included graphs regarding the impact on leverage, total debt outstanding, and rate pressure by rate period.[303] BPA has discussed its concerns with Transmission's unsustainable debt trajectory and net borrower status throughout this process, in addition to numerous other considerations. The first grounding workshop, on October 19, 2021, began by explaining BPA's objectives to reduce interest expense, maintain financial flexibility, and maintain access to secure and low-cost debt financing.[304] This workshop also discussed BPA's total outstanding debt, Transmission's increasing debt profile, total projected interest expense, forecasted remaining borrowing authority, historical and projected debt-to-asset ratios, credit rating perspectives, and industry practice for capital financing and leverage ratios, and identified Transmission's net borrowing position as a "key issue." BPA reiterated these points at the January 26, 2022, workshop before presenting an initial approach for discussion.[305] The initial approach included a goal to "achieve at least a net neutral borrowing position over a rolling 10 year period."[306] BPA removed this as a separate goal in its Policy, not because the agency believes the goal unimportant, but because it added unnecessary complexity when achieving net neutral borrower status "is an outcome of achieving our [60% by 2040] leverage goal."[307] "A net neutral borrowing position will arrest the growth of Transmission's debt and ensure a more consistent cost of service over time, rather than requiring future rates to deal with an ever increasing debt service load."[308]

At the May 24, 2022 workshop, BPA Staff explained that BPA selected these goals for a number of reasons, including:

- Achieving these goals will improve BPA's financial flexibility and help to ensure a consistent cost of service over the long-term.

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[300] Comment Response Compilation at 64-67.
[301] NIPPC *et al.* Comments at 3 n.9.
[302] *Id.*
[303] Comment Response Compilation at 64-67.
[304] Oct. 19 Presentation at 7-8.
[305] Jan. 26 Presentation at 8-17.
[306] *Id.* at 12.
[307] Comment Response Compilation at 62; *see also* May 24 Presentation at 6.
[308] Comment Response Compilation at 34.

- Our purpose is not to improve BPA's credit rating, although we recognize revenue financing can be viewed as credit supportive.
- Grounded in industry practices: We have compared and contrasted the practices of other entities that are comparable, yet distinct, to ensure our revenue financing approach is reasonable.
- Long-term horizon: Driving toward the goal over a 20-year horizon enables development of an approach that puts rate impact considerations at the forefront.
- Alignment with industry norms: Targeting a debt to asset ratio in the 40% to 60% range is common practice. Our goal of 60% puts us at the upper end of this range, achieved over a 20-year horizon.
- Prudent debt management: 60% leverage results in significant avoided interest expense, lowering future fixed costs, and is the target needed to flatten Transmission's outstanding debt level over time.[309]

These were all considerations in developing the parameters of our Sustainable Capital Financing Policy. A 70 percent target, as compared to BPA's Policy, would forego or significantly reduce the magnitude of many of the long-term benefits BPA seeks to achieve. Transmission will become a net neutral borrower as a result of BPA's Policy goal; it would not with a goal for 70 percent leverage by 2040. Allowing Transmission's net borrower status to continue would result in its debt to continue to grow at an unsustainable pace, and make the issue more difficult to address in the future. This additional debt burden would result in higher fixed costs, less financial flexibility, and less of a hedge against increased interest expense risk. BPA has balanced these long-term benefits with the near-term rate impact through a rate impact limiter, flexibility to respond to circumstances, and the intent to repurpose revenue financing for liquidity in poor financial years. In the context of this Policy, the goal to achieve debt-to-asset ratios no greater than 60 percent by 2040 appropriately balances these considerations.

Decision

BPA's goal to achieve agency and business unit debt-to-asset ratios no greater than 60 percent by 2040 is a reasonable goal (1) as confirmed by comparisons to similar, but distinct, entities; (2) that will be viewed as a credit positive; (3) that considers the potential near-term impact in achieving long-term benefits; (4) that allows BPA to respond to industry change; and (5) more appropriately balances the near- and long-term impacts than alternative proposals.

[309] May 24 Presentation at 6.

Issue 4.2.3.2

Whether BPA should calculate default amounts of revenue financing using forecast or actual IPR capital spending.

Public Comments

PPC notes that its "initial comments expressed support for planned revenue financing based on actual instead of planned capital spending . . . based on the historical trend of significant underspending of planned capital budgets."[310] PPC asserts, "[t]his concern is generally mitigated by BPA's adoption of target ranges for capital spending relative to planned amounts in rates."[311] "However," PPC notes, "if substantial underspending continues, it may be necessary to revisit the planned versus actual capital spending issue."[312]

Several commenters expressed concern with BPA historically under-spending its forecast Transmission capital budget.[313] They argue that the use of forecast IPR capital spending to calculate default amounts of revenue financing will result in BPA over-collecting unjustified revenue financing from its customers.[314] MSR calculates that, based on the amount of underspending in FY 2021, "[a]pplying BPA's proposed 10% revenue financing would have caused an excess $10 million of revenue financing for Transmission, and $8 million for Power."[315] Powerex argues that, under the Policy, underspending "would result in rate pressure based on projects that are not completed in the forecasted period."[316] Avangrid *et al.* assert that, by using forecasts, "BPA would be arbitrarily including in revenue requirement revenue financing for capital spending that did not occur."[317]

Avangrid *et al.* offer two proposals for calculating the default amounts of revenue financing, with their preference for the first.[318] First, they propose "calculating revenue financing amounts, if any, using the lesser of the most recent actual capital spending amounts and the IPR capital spending forecasts [to] avoid (i) basing revenue financing on BPA over-forecasts of capital spending, and (ii) basing revenue financing on the most recent actual capital spending amounts that exceed BPA's capital spending forecasts."[319]

Second, Avangrid *et al.* propose, "BPA should at least true-up for any over-forecast of capital spending through a reduction of revenue requirement in the next BPA rate case."[320] They clarify, "[s]pecifically, if there is any increase in revenue financing for a rate period due to an over-forecast of capital spending, the revenue financing for the next rate period

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310 PPC Comments at 2.
311 *Id.*
312 *Id.*
313 AWEC Comments at 3; Avangrid *et al.* Comments at 4-5; MSR Comments at 12; Powerex Comments at 2.
314 AWEC Comments at 3; Avangrid *et al.* Comments at 5; MSR Comments at 13.
315 MSR Comments at 12-13.
316 Powerex Comments at 2.
317 Avangrid *et al.* Comments at 5.
318 *Id.* at 4-5.
319 *Id.* at 5.
320 *Id.*

should be decreased by the amount of such increase in revenue financing due to the over-forecast."[321]

Evaluation

BPA recognizes and is addressing the historical variance BPA has seen between rate case capital forecasts and execution. This topic was discussed at the March 9 Workshop as part of the broader Financial Plan Refresh process. There, BPA Staff stated, "BPA is committed to explaining the drivers of variance between forecasts and actuals at the QBR technical workshops, and as needed, making process improvements."[322] Staff explained variance could be due to reprioritization of projects (*e.g.,* due to critical and emerging business needs); changes in staffing, material, parts, equipment availability, or outage availability, which can impact project schedules and milestones; or changes in project costs since forecast (*e.g.,* due to implications from the pandemic and associated supply chain challenges).[323] At that Workshop, PPC and Snohomish gave a presentation advocating for certain capital planning and execution metrics.[324] BPA intends to address commenters' concerns at the source by modifying how it develops its forecasts, what amounts are included in rates, and how it tracks success.

BPA bases its capital forecasts on its asset management strategy described in its Strategic Asset Management Plans (SAMPs). As part of its asset management program, BPA regularly reviews historic expenditures compared to the original forecast to better understand the reasons for underperformance compared to planned levels, and develops approaches to mitigate the issue. An example of this is the Secondary Capacity Model (SCM), now being used by Transmission Services, which is designed to remove some of the bottlenecks in the construction program and improve execution. Further, as BPA works to mature its asset management program and strengthen capital performance, BPA has created a mid-point budget to be used in BP-24 for federal hydro facilities and Transmission. The mid-point budget is 10 percent less than expected capital level needs; adopting this approach helps to ensure our capital forecast in rates is more in line with historic performance. At the same time, these asset categories will strive to hit the higher target outlined in the SAMP, further reducing the risk of executing below the level included in rates.

As a result of using a lower capital forecast while still working to achieve the higher forecast, BPA is changing its Key Performance Indicator (KPI) from defining success as being below 100 percent of forecast, to now defining success as being within a certain percentage, plus or minus, of the forecast. BPA would still report this KPI as "green" if actuals are over (or under) the rate case forecast amount, as long as the execution is within the banded range. BPA intends to use its QBR Technical workshops to report out on capital performance and capital metrics.

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[321] *Id.*
[322] Mar. 9 Presentation at 6.
[323] *Id.*
[324] PPC and Snohomish, *Capital Planning and Execution Metrics* (Mar. 9, 2022), https://www.bpa.gov/-/media/Aep/finance/financial-plan-refresh/20220309-ppc-snohomish-capital-planningpand-execution-metrics.pdf.

As a practical matter, all revenue financing would still be used to fund actual capital investments, unless repurposed for liquidity. As with all forecasts, actuals will vary. Assuming the default amount was 10 percent of a business unit's forecast capital spending, if actual capital spending is higher than forecast, then revenue financing would be less than 10 percent. If actuals are lower than forecast, then revenue financing would be higher than 10 percent.

However, this assumes that actual revenue financing would equal the forecast amount included in rates. This will not always be the case. The Policy includes provisions to repurpose revenue financing for liquidity. Section 6 states:

> [W]hen a business unit's start-of-year reserves for risk are between 60 and 120 days cash on hand, BPA intends that revenue financing will be reduced to the extent that a business unit's end-of-year reserves for risk are expected to be lower than the start-of-year. The reduction is limited to the amount needed to retain the start-of-year reserves for risk.[325]

If this occurs, actual revenue financing would be less than 10 percent of forecast capital spending. If the default amount was revised to reflect a prior year's actual capital spend, it would make sense to also reflect the prior year's actual revenue financing. Avangrid *et al.*'s "lower of" proposal recognizes that actual capital spending could be higher than forecast, but it is not clear why it would then be inappropriate to base "revenue financing on the most recent actual capital spending amounts that exceed BPA's capital spending forecasts."[326]

Rather than require the default amount of revenue financing to increase or decrease to reflect the prior rate period's actuals, BPA will use forecasts. This simple approach is consistent with BPA's practice of forecasting nearly all values used in setting its rates, and provides a direct line of sight from the IPR and SAMP forecast capital levels. Moreover, using forecast capital avoids potential complexity in (1) having to update the default amount from initial to final proposal within a rate case to reflect the most recent prior year's actuals, and (2) using actuals to calculate the 10 percent or 20 percent of capital spending and forecasts to calculate whether a business unit is expected to achieve 60 percent leverage by 2040.

Notably, while BPA will calculate the default amount using forecasts, the Policy allows flexibility to respond to circumstances. This flexibility specifically includes the ability to respond to circumstances including the "likelihood of achieving the debt-to-asset ratio policy goal" and "whether an amount of revenue financing greater or less than the default amount occurred in a prior rate period."[327] If actual capital spending were—over time and despite BPA's best efforts to address variance concerns through capital prioritization and performance metrics—to be significantly below forecast, and revenue financing is not repurposed for liquidity, Transmission would be more likely to achieve 60 percent leverage by 2040.

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325 Attachment 1, Sustainable Capital Financing Policy § 6.
326 Avangrid *et al.* Comments at 5.
327 Attachment 1, Sustainable Capital Financing Policy § 5.

Calculating default amounts using forecasts is simple and consistent with BPA's practice. BPA continues to take actions to directly mitigate the concerns driving commenters' alternate proposals. In the event that actuals significantly vary from forecast, the Policy includes flexibility for BPA to respond appropriately.

Decision

BPA will calculate default amounts of revenue financing using forecast IPR capital spending.

4.2.4 Rate Impact

Issue 4.2.4.1
Whether BPA appropriately considered the rate impact of its policy.

Public Comment

Snohomish supports the Sustainable Capital Financing Policy "as a means to achieve a 'more stable cost of service over time.'"[328] The Policy provides "a roadmap to achieve the objective and sets parameters to mitigate the uncertainty over revenue financing which was the impetus that started the Financial Plan Refresh."[329]

WPAG states, "BPA has made a compelling case that continuing to debt finance 100% of the capital program is unsustainable."[330] WPAG supports including "a default amount of 10% revenue financing for each business unit with a cap of 20% if achievement of the debt-to-asset ratio goal for 2040 is in doubt,"[331] and "limit[ing] the amount of incremental revenue financing from rate period to rate period at $15 million for Transmission and $25 million for Power."[332]

Powerex "generally supports actions that result in lower and stable transmission rates," but argues "Bonneville has not given appropriate attention to the rate impacts of its draft policy, and rate impact assessment and analysis on the effects of long-term rate increases to long[-]term investments made by transmission customers."[333] Powerex calculates the total expected revenue financing between now and 2040, subtracts the avoided interest expense over that time period, and divides the amount evenly over that period to conclude that "[t]his revenue financing would represent roughly an 8-9 percent increase in Transmission rates each rate period."[334] "Further," Powerex asserts, "this magnitude of revenue financing suggests that the default amount under the draft policy would never be 10 percent . . . ."[335]

MSR argues the Policy "would add at least $55 million to Transmission's annual revenue requirement, and $65 million to Power's annual revenue requirement[, which] amounts to

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328 Snohomish Comments at 1.
329 *Id.*
330 WPAG Comments at 1.
331 *Id.*
332 *Id.*
333 Powerex Comments at 1-2.
334 *Id.* at 2.
335 *Id.*

rate increases of roughly 5.5% and 3.2%, respectively, for Transmission and Power, before any other rate pressures are considered."[336] MSR argues that "adding an unnecessary 5.5% and 3.2% increase" is unreasonable.[337] MSR notes that "BPA is discussing an $80 million annual Transmission cost increase [that] is nearly twice the increase designed under BPA's policy of limiting IPR cost increases to the rate of inflation" and calculates that "[t]he combination of the IPR costs and the revenue financing proposed in the Draft Policy appears to total a double-digit rate increase of about 13.5% for all Transmission customers (in addition to sharply rising costs of energy in the market)."[338]

MSR proposes BPA "develop a limit that takes other cost increases into account, deferring any revenue financing if rates would increase more than the rate of inflation[, which] would respect BPA's existing cost control policy."[339] In a footnote, Avangrid *et al.* suggest "[o]ne possible way to ameliorate or at least mitigate the cumulative impact would be for BPA to establish in the Financing Policy a cumulative cap over a set period of years in addition to its '1% cap' ($15 million per year for Transmission Services or $25 million per year for Power Services)."[340]

Relatedly, NIPPC asserts that "a major weakness that needs consideration is the BPA cash revenue financing proposal would use cash today to fund capital which has the effect of putting pressure on available liquidity."[341] Given that "BPA's most significant operating risk is a drought affecting power production," NIPPC states that "[s]ignificant reserves to manage volatility in low water years is an important financial strategy which should be maintained."[342]

<u>Evaluation</u>

BPA designed this Policy to achieve the long-term benefits of revenue financing a portion of its capital program, and carefully considered how best to balance the near-term rate impact. The Policy sets parameters to guide financing decisions on an annual $800 million to $1 billion capital program, with a nearly 20-year timeline to get on course. Without change, Transmission is currently projected to borrow $2 billion more than it repays over that timeframe, largely on maintaining its existing assets. This Policy addresses large scale issues.

Regarding Powerex's requests for additional analysis, BPA does not forecast rates prospectively. BPA's rates are designed to recover its costs, currently over a two-year timeframe. It would be speculative to attempt long-term rate forecasts. BPA did share its

336 MSR Comments at 5.
337 *Id.*
338 *Id.*
339 *Id.* at 13.
340 Avangrid *et al.* Comments at 4 n. 11.
341 NIPPC Comments at 4.
342 *Id.*

analysis concerning the *incremental* cost and rate implications of its initial approach and provided additional analysis for achieving a 70 percent debt-to-asset ratio by 2040.[343]

Powerex's analysis assumes BPA would 100 percent debt finance without the Policy, and focuses only through 2040. Powerex takes the amount of revenue financing expected under the policy through 2040 and levelizes it equally over that time period. Assuming that $15 million results in a 1 percent rate increase, this levelized approach would result in an approximately 8.6 percent[344] rate increase in BP-24, and no incremental rate impact through 2040. Powerex characterizes this as "roughly an 8-9% increase in Transmission rates each rate period."[345] BPA chose to shape the parameters of the Policy to consider near-term rate impact and avoid this result.

Although Powerex and MSR compare rate impacts under this Policy against a default assumption of 100 percent debt financing, this is not appropriate. Section 2.6 and Issues 4.2.2.1 and 4.2.3.1 discuss why BPA is moving away from the unsustainable practice of 100 percent debt financing. In the absence of a Policy, BPA would still make capital financing decisions on a rate-case by rate-case basis. Sustained 100 percent debt financing is not a sure point of comparison to evaluate the impact of this Policy.

Powerex's analysis does not fully account for the significant interest savings of revenue financing that will continue to accrue and compound. Even if BPA decided to abandon this Policy in 2040, and to 100 percent debt finance its capital program thereafter, the benefits of avoided interest expense between now and 2040 would continue to accrue. Assuming the alternative to revenue financing $1.75 billion of Transmission capital program was to finance this capital with a 30-year bond at a 3.75 percent interest rate, the interest expense savings over the life of those bonds is roughly $600 million. This interest rate is low, and even modest increases in interest rates would significantly increase these savings.[346] For example, if BPA's borrowing cost rises to 5.50 percent over the next five years, and stays at this level through 2040, the avoided interest savings grows to nearly $845 million for Transmission customers. Given that financing decisions will not change the principal portion spent on BPA's capital program, these interest savings represent an overall net benefit that would be forfeited by 100 percent debt financing.

BPA has been mindful of the Policy's near-term impact, and has structured this Policy to achieve its objectives and long-term benefits with no greater than approximately 1 percent incremental rate impact from rate period to rate period, or 0.5 percent per year, with Power not expected to see any incremental rate impact. As for Powerex's assertion that Transmission's default amount "would never be 10 percent,"[347] Transmission would begin revenue financing 10 percent when doing so results in a business unit debt-to-asset ratio no greater than 60 percent by 2040 on a forecast basis.

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343 Comment Response Compilation at 64-67.
344 Powerex Comments at 2 n.6-7.
345 *Id.* at 2.
346 *See* Jan. 26 Presentation at 14-16 ("Why These Goals are Important – Hedging Risk").
347 Powerex Comments at 2.

BPA will not adopt MSR's proposal to require revenue financing be reduced if rates would increase more than the rate of inflation,[348] or Avangrid *et al.*'s suggestion for a "cumulative cap."[349] BPA has included flexibility to deviate from the default amount of revenue financing in certain circumstances, including "rate pressure."[350] Instead of adding mechanical requirements for how BPA must respond to each of those circumstances, BPA will allow current circumstances to be balanced within each rate case.[351]

Finally, regarding NIPPC's concern that revenue financing "would use cash today to fund capital which has the effect of putting pressure on available liquidity,"[352] BPA would not draw from existing financial reserves, but would include an amount of revenue financing in rates to finance new capital. BPA's liquidity is managed under the FRP, risk adjustment mechanisms, and the TPP Standard. This Policy is explicitly liquidity-supportive, including the intent to repurpose revenue financing for liquidity when reserves levels are expected to decline.[353]

Decision

BPA appropriately considered the near-term rate impact of the Sustainable Capital Financing Policy in order to achieve long-term benefits and objectives.

Issue 4.2.4.2

Whether a 1 percent incremental rate impact limiter should be added to scenarios where the default amount of revenue financing is 10 percent of the IPR capital financing forecast.

Public Comments

AWEC "is concerned about the optionality for a default level of revenue financing in each rate period to be calculated as part of the IPR process."[354] More specifically, "[t]he concern is the level of rate impact that may be experienced under the 10 percent of IPR capital spending forecast [scenario] . . . ."[355] AWEC states, "[i]t is unclear why the 10 percent of capital scenario of revenue financing is not subject to a one percent rate increase cap, while the alternative is subject to an implicit one percent cap."[356] AWEC argues that "the level of revenue financing for each rate period should not exceed a one percent impact regardless the level [of] revenue financing."[357]

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348 MSR Comments at 13.
349 Avangrid *et al.* Comments at 4 n. 11.
350 Attachment 1, Sustainable Capital Financing Policy § 5.
351 *See infra* Issues 4.2.5.1 and 4.2.5.3.
352 NIPPC Comments at 4.
353 Attachment 1, Sustainable Capital Financing Policy § 6.
354 AWEC Comments at 3.
355 *Id*.
356 *Id.*
357 *Id.*

Evaluation

BPA's policy includes the goal of moving away from 100 percent debt financing by revenue financing a portion of capital.[358] Under this Policy, BPA intends to revenue finance 10 percent of its capital program. However, if forecasts show that 10 percent revenue financing is not enough for a business unit to achieve 60 percent leverage by 2040, then more revenue financing is added to get back on track.[359] While the Policy calls for such a business unit to revenue finance more, BPA considered how to manage near-term rate impact while still achieving the long-term objective over time. In such scenarios, Section 5.2 in the Policy strikes this balance by setting the default amount of revenue financing at the lower of 20 percent of the IPR capital spending forecast or approximately 1 percent incremental revenue financing.[360]

BPA does not expect scenarios where revenue financing 10 percent of the capital program will result in greater than 1 percent incremental rate impact. The analysis shows that Power's revenue financing will be roughly stable compared to the $40 million per year in the BP-22 rate case settlement.[361] Revenue financing changes by about $2 million per year per rate period, which produces far less than a 1 percent incremental effect on rates. As a result, a 1 percent incremental rate impact limiter would provide no benefit for Power at 10 percent revenue financing. For Transmission, the analysis shows that it is not forecast to achieve the goal of 60 percent leverage by 2040 with just 10 percent revenue financing. As a result, a rate limiter at 10 percent revenue financing would be of no value to Transmission. Since Transmission is not expected to be at the 10 percent level, and Power's revenue financing is expected to stay at roughly $40 million per year, there is no need for an incremental rate impact limiter at this level of revenue financing. Nonetheless, the Policy includes flexibility to respond to circumstances, including "rate pressure," "likelihood of achieving the debt-to-asset ratio policy goal," and "whether an amount of revenue financing greater or less than the default amount occurred in a prior rate period."[362] Regardless of the default amount calculated in the IPR process, BPA may propose or adopt—and customers may advocate in the rate case for—a different amount based on the circumstances.[363]

Decision

BPA will not add a 1 percent incremental rate limiter where the default amount of revenue financing is 10 percent of the IPR capital financing forecast.

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358 Attachment 1, Sustainable Capital Financing Policy § 4.1.
359 *Id.* § 5.2.
360 *Id*.
361 Jan. 26 Presentation at 21.
362 Attachment 1, Sustainable Capital Financing Policy § 5.
363 *See supra* Issue 4.2.5.3.

4.2.5 Policy Implementation

Issue 4.2.5.1

Whether the flexibility within the Policy to deviate from default amounts of revenue financing is appropriate.

Public Comments

Snohomish "supports the . . . flexibility embedded in the Draft Sustainable Capital Financing Policy."[364] WPAG "is supportive of many elements of BPA's revenue financing proposal, including BPA's proposals to . . . [r]etain the flexibility to reduce or eliminate revenue financing for a given rate period to respond to changing circumstances including, importantly, in response to other rate pressures."[365] NIPPC *et al.* "appreciate the flexibility in the Draft Plan for less revenue financing in the event of changes in BPA's capital program, which we understand could encompass a higher capital spending for upgraded transmission capacity, including new lines [and] urge the Administrator to retain this flexibility in any final policy."[366]

NRU, PPC, and WPAG propose additional constraints on the ability to revenue finance more than the default amount. NRU does not support the policy's flexibility, and "recommends an amendment to the proposed policy that would allow BPA to use its discretion to propose less revenue financing than the default amount or allow BPA to propose more revenue financing solely if the revenue financing would yield a net or negative rate impact."[367] NRU explains this amendment "would provide additional certainty to preference customers about the rate impact of revenue financing over time and additional comfort with BPA's implementation of the revenue financing policy."[368] While PPC "appreciates and supports the need for flexibility in the Sustainable Capital Financing Policy," it proposes "the final policy should contain clear language that any additional revenue financing must have a clear rate benefit to customers."[369] WPAG "recommends that BPA amend the draft policy to limit BPA's ability to exceed the $15 million for Transmission and $25 million for Power incremental limits to additional revenue financing beyond the amounts in the then current rates to only those circumstances where there is strong support on the record from customers in the subject rate case."[370]

AWEC "finds necessary and supports" BPA including flexibility to respond to "circumstances includ[ing] things like triggering of risk adjustment mechanisms and rate pressure," but is concerned "that the decision to exercise flexibility is left entirely to BPA, including whether it will nevertheless insist on a level of revenue financing that would lead to a greater than one percent rate impact."[371]

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[364] Snohomish Comments at 1.
[365] WPAG Comments at 1.
[366] NIPPC *et al.* Comments at 4.
[367] NRU Comments at 2.
[368] *Id.*
[369] PPC Comments at 2.
[370] WPAG Comments at 1.
[371] AWEC Comments at 3.

Evaluation

As discussed in Issue 4.2.5.3, BPA will justify and support any amount of revenue financing it includes in rates with evidence in the record, including proposals to deviate from the Policy's default amounts of revenue financing. Parties in the rate case will be able to advocate for their positions. It may be appropriate, based on the circumstances, to decrease revenue financing below the default amount in a given rate period, and then increase revenue financing above the default amount in a subsequent rate period. BPA does not agree to place a higher hurdle on the flexibility to increase—as opposed to decrease—revenue financing from the default amount. Instead, it is sufficient that the amount be justified by evidence on the record.

Decision

BPA will not add restrictions on the Policy's flexibility; BPA will retain flexibility within the Policy to deviate from default amounts of revenue financing to respond to circumstances in each rate case.

Issue 4.2.5.2

Whether BPA should defer adopting the Policy or commit to revisit the Policy in the near term.

Public Comments

Snohomish and PPC expect continued engagement from BPA. Snohomish appreciates "the amount of work invested by [BPA] to fulfill the commitment set forth in the BP-22 settlement for a Financial Plan Refresh," "the opportunity to actively participate in this important process," and " the Agency's acknowledgment that continued collaboration is necessary to understand the interplay between the policy and Post-2028 considerations."[372] PPC states: "[t]he current BPA proposals substantively address most of the sideboards and considerations in PPC's initial comments, including . . . the need for openness to changes if needed to accommodate developments in the post-2028 process."[373] And while PPC "would support the NIPPC proposal to begin with a target for 70% with a defined check in to see if moving to a more aggressive value is appropriate," PPC states, "[a]lternately, in several rate periods as circumstances change, we encourage BPA to maintain openness to new information on appropriate long-term leverage targets."[374]

Powerex, NIPPC, OPUC and WUTC, and PNGC argue that BPA should defer adopting the Policy. Powerex "understands the need to responsibly manage debt, but . . . believes the draft policy requires further review and is not ready for adoption."[375] OPUC and WUTC "believe it is imperative that BPA articulate a compelling need for such a change at this time, something that in our opinion it has not done so far, and to fully engage stakeholders on possible alternatives."[376] They "did not observe a substantial effort to use the workshop

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372 Snohomish Comments at 1-2.
373 PPC Comments at 1.
374 *Id.* at 2.
375 Powerex Comments at 1.
376 OPUC and WUTC Comments at 1.

process to engage regarding other leverage target levels or explore the viability of alternatives" and "encourage the Administrator to take some more time to engage with its transmission customers and explore alternatives before reaching a final decision."[377] NIPPC argues that "[w]ith greater inflation and interest rate risk in the next year, a pause on BPA's proposal should be established with a re-examination in two years."[378] PNGC "does not think revenue financing is necessary at this time and has suggested that it should be deferred to the post-2028 negotiation and that major financial policies and decisions should be part of that negotiation and final contract structure."[379]

Powerex, NIPPC *et al.*, NRU, AWEC, and WPAG offer various proposals related to a commitment by BPA to revisit the Policy. The latter four tie their proposal to post-2028 contract negotiations. Powerex proposes BPA should "consider an automatic review of the policy after each rate period to ensure it is achieving the stated objectives, while providing an opportunity for customer input."[380] Further, Powerex proposes BPA should "also consider adding an automatic review and sunset provisions if the policy is not achieving the desired goals or is unduly impacting customers with rate pressure."[381] As discussed in Issue 4.2.3.1, NIPPC *et al.* propose BPA modify its goal to instead target a debt ratio of 70 percent by 2040, with "[p]lanned reconsideration of this 70% target in 4 years (2026), including evaluation of whether adopting a 60% alternative long-term target would be more financially sound."[382]

NRU "strongly recommends that BPA should commit in its policy to a reconsideration process of its revenue finance policy with customers in four years to (1) review the leverage ratio goal of 60% debt-to-asset ratio by 2040 and determine whether the leverage target of 60% and timeframe of the goal result in a reasonable impact for customers, and (2) incorporate policies outlined in the post-2028 Contract Policy Record of Decision due to be released September of 2025 into BPA's financial policy."[383] AWEC "continues to be concerned about the interaction between BPA's Financial Plan Refresh proposals and the post-2028 Provider of Choice contracts [and] further recommends that these policies be revisited ahead of the post-2028 contract period once more is known about the nature of the contractual and rate relationship customers will have with BPA in the future."[384] WPAG notes that the Public Power Post-2028 Concept Paper "recommends that the next contracts should set the financial policies that will be in place during the term of the contract and that any amendments or additions thereto should be limited to only those that are agreed to by BPA and a super-majority of its preference customers," and therefore "recommends that BPA should revisit both the Capital Financing Policy and Financial Plan with stakeholders ahead of post-2028 contract period."[385]

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377 *Id.* at 1-2.
378 NIPPC Comments at 4.
379 PNGC Comments at 1.
380 Powerex Comments at 1.
381 *Id.* at 2.
382 NIPPC *et al.* Comments at 3.
383 NRU Comments at 1-2.
384 AWEC Comments at 4.
385 WPAG Comments at 2.

Evaluation

BPA's process for adopting this Policy was robust. On September 15, 2021, BPA held its Financial Plan Refresh Kick-Off public workshop. Since then, as detailed in Section 2.8, BPA has held numerous public workshops, considered and responded to public comments and presentations, and performed additional analysis. This collaboration informed our draft Policy, and provided stakeholders with notice and opportunity to comment. Having considered the arguments in this ROD, BPA believes the Sustainable Capital Financing Policy should now be adopted.

In response to a prior customer recommendation for BPA to revisit the Policy in the near term due to post-2028 contract considerations, BPA Staff stated:

> We recognize that BPA's financial policies will influence customer consideration of post-2028 contracts. While we are not planning a comprehensive financial policy review ahead of the next long-term power sale offering, we acknowledge that a fundamental change to risk volatility might warrant revisiting existing interrelated policies. Over the past six months, our current effort has sought to engage with stakeholders to develop a policy that is durable in making measured progress towards our long-term goals and in allowing flexibility within the policy to respond to changing circumstances. We understand that the interplay between BPA's financial policies and the post-2028 contract conversation is an important issue and we look forward to continuing the dialogue on this topic.[386]

While BPA will not commit to sunset the Policy at a certain date and start a new policy development process from scratch, our intent is in line with PPC's encouragement to "maintain openness to new information on appropriate long-term leverage targets."[387] As BPA has stated before, "[w]e agree that periodic review of the policy, goals and metrics is . . . prudent, and aligns with the standard business practice of 'plan, do, check, and adjust.'"[388]

BPA intends to periodically review this Policy and receive stakeholder input to ensure it is operating effectively. The agency believes a cadence of approximately every five years is appropriate. BPA also recognizes that predictability and consistency are important aspects of a durable long-term capital financing policy. To highlight its intent, BPA has decided to state it within the Policy itself. A new section has been added to the Sustainable Capital Financing Policy, which states:

> The intent of this Policy is to provide durable guidance on capital financing decisions for long-term debt management. BPA intends to periodically review this Policy to consider its progress toward achieving the goals set forth in Section 4, to ensure the Policy is operating effectively, and to ensure the Policy continues to align with BPA's strategic direction. BPA will request stakeholder

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386 Comment Response Compilation at 54.
387 PPC Comments at 2.
388 Comment Response Compilation at 30.

input as part of this review. BPA expects to review the Policy approximately every five years.

BPA will also monitor and annually report its progress toward meeting the Policy goals.[389]

Decision

BPA's process for adopting this Policy was adequate. BPA will modify its draft Policy to include a section regarding its intent to conduct periodic review approximately every five years.

Issue 4.2.5.3

Whether adoption of the Policy preempts or supplants the procedural requirements of the Northwest Power Act to support a decision to include revenue financing in rates with evidence in the rate case record.

Public Comments

Avangrid *et al.* argue that the goals of the Policy and the "default amount" of revenue financing constitute a "general statement of policy" by BPA that cannot "preempt or supplant" the Northwest Power Act requirements to develop a full and complete record to justify the amount of revenue financing in a particular rate case.[390] Avangrid *et al.* maintain that BPA must justify the proposed amount of revenue financing on the record in each rate case. The parties recommend modifying the Policy to avoid the "arbitrary and capricious" result of adopting the default amount of revenue financing when that amount would be "unreasonable" based on the record.[391]

Powerex states that the Policy is an "interpretive rule or non-binding statement of general policy" and that it expects BPA to justify "revenue financing proposals with a full and complete record in each rate proceeding" pursuant to the requirements of the Northwest Power Act.[392]

Evaluation

BPA developed the Policy, including the "default amount" of revenue financing, with the procedural requirements of Section 7(i) of the Northwest Power Act in mind.[393] Although the adoption of the Policy makes clear that BPA intends to apply the Policy to the development of revenue financing proposals in future rate cases, it does not alter the requirement that the Administrator must ultimately decide the issues in those rate cases based on the evidentiary record in the proceeding.

Avangrid *et al.* are concerned with the statement that the policy establishes "binding precedent" for future rate cases and that the Policy may provide only limited opportunity

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[389] Attachment 1, Sustainable Capital Financing Policy § 7.
[390] Avangrid *et al.* Comments at 3-4.
[391] *Id.*
[392] Powerex Comments at 3 n. 9.
[393] 16 U.S.C. § 839e(i) (2020).

to deviate from the default amount of revenue financing "even when the record supports a different result."[394] The commenters argue that BPA is issuing a "general statement of policy" and that by law an "agency cannot rely upon a general statement of policy as binding precedent."[395] The parties maintain that adopting a policy with a "pre-determined 'default amount' of revenue financing that BPA may deviate from only in 'extraordinary circumstances' appears to ignore the fact that any amount of revenue financing . . . must be justified and fully supported in the record" and consistent with the applicable statutory standards.[396] Powerex expresses similar concerns.[397]

BPA has developed the Policy with the procedural requirements of its rate proceedings in mind. BPA rate proceedings start with the release of BPA's "initial proposal" for rates, which includes extensive studies and testimony that BPA has developed before the proceeding to explain and support the proposal. Over the course of the proceeding, parties have the opportunity to submit testimony and other evidence regarding the issues in the initial proposal. At the end of the proceeding, the Administrator decides the issues based on the evidence in the record developed in the proceeding.

BPA's adoption of the Policy does not change this process with respect to addressing any revenue financing proposal. BPA will develop a proposed amount of revenue financing in accordance with the Policy, and include that amount in its initial proposal for rates. BPA expects that, in most circumstances, its initial proposal will include the default amounts of revenue financing provided for in the Policy. Parties will then have the opportunity to submit testimony and evidence regarding the amount of revenue financing that BPA has proposed. The Administrator will ultimately decide the issue based on the evidence in the record as a whole.

BPA finds merit in Avangrid *et al.*'s concern with the Policy's use of the term "extraordinary circumstances."[398] BPA did not intend to set a standard that would "preempt or supplant the requirement for a full and complete justification of BPA rates in the BPA rate case record of decision pursuant to section 7 of the Northwest Power Act."[399] The term "extraordinary circumstances" was not meant to limit BPA from deviating from the Policy's default amounts when the record supports doing so. Instead, it reflects BPA's expectation that it will initially propose the default amounts in most circumstances. As explained in this ROD, the default amounts are designed to balance long-term benefits and objectives with near-term rate impact and intergenerational equity. BPA also recognizes that a lack of consistency would affect these considerations, and therefore counsels against deviating from the default amounts. The existence of the Sustainable Capital Financing Policy, which is designed to achieve the agency's objectives while balancing competing considerations, and the accompanying ROD, will be relevant evidence in making such decisions.

[394] Avangrid *et al.* Comments at 3.
[395] *Id. citing Pac. Gas & Elec. Co. v. Fed. Power Comm'n*, 506 F.2d 33, 38-39 (D.C. Cir. 1974).
[396] *Id.*
[397] Powerex Comments at 1, 3 n. 9.
[398] Avangrid *et al.* Comments at 3-4.
[399] *Id.*

Nonetheless, the amount of revenue financing in the initial proposal will provide a starting point for the submission of testimony and evidence on BPA's proposal. Even if the initial proposal includes the default amount of revenue financing provided for in the Policy, the Policy does not preclude parties from submitting testimony and evidence recommending the Administrator adopt a different amount based on current circumstances.

BPA has conducted an extensive public process with multiple opportunities for stakeholders to submit comments on BPA's evidence and proposals, resulting in this ROD. The record supports a policy to take steps to move away from 100 percent debt financing by revenue financing a portion of capital and achieve agency and business unit debt-to-asset ratios of no greater than 60 percent by 2040, and sets reasonable parameters to achieve those goals.

Finally, we note that the process for adoption of the policy statement at issue in the *Pacific Gas and Electric* decision cited by Avangrid *et al.* differs dramatically from the process that preceded the Policy BPA is adopting in this ROD.[400] The Federal Power Commission adopted the policy statement in *Pacific Gas and Electric* without any prior notice or opportunity for comment.[401] In addition, in the policy statement, the Commission expressly reserved the right of parties to "challenge or support th[e] policy through factual or legal presentation as may be appropriate in the circumstances presented."[402] The Sustainable Capital Financing Policy, and the rationale for its adoption in this ROD, will be relevant evidence in future rate case proceedings.

Decision

Adoption of the Policy does not preempt or supplant the procedural requirements of the Northwest Power Act. BPA will modify the Policy language to clarify its intent. BPA will justify and support any amount of revenue financing it includes in rates with evidence in the record in the rate proceeding, but the Sustainable Capital Financing Policy, and the rationale for its adoption in this ROD, will be relevant evidence in such proceedings.

4.3 Out-of-Scope Comments

A few commenters submitted comments outside the scope of this process. BPA notes these comments here, but does not respond to them as they are beyond the scope of BPA's decision to adopt the Sustainable Capital Financing Policy.

Snohomish submitted comments concerning use of the RDC.[403]

AWEC submitted comments supporting BPA's operational liquidity.[404]

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[400] *See Pac. Gas & Elec. Co.*, 506 F.2d at 36. The Court in *Pacific Gas and Electric* notes that the distinction between substantive rules and general statements of policy is a "fuzzy product." *Id.* at 37.
[401] *Id.*
[402] *Id*. at 40 (quoting *Utilization and Conservation of Natural Res.—Natural Gas Act*, 49 F.P.C. 85 (Jan. 8, 1973)).
[403] Snohomish Comments at 2.
[404] AWEC Comments at 4.

MSR and PNGC submitted comments regarding BPA's "higher of" methodology and "technical accounting concerns."[405]

5. NATIONAL ENVIRONMENTAL POLICY ACT ANALYSIS

Consistent with the National Environmental Policy Act (NEPA), 42 U.S.C. § 4321, *et seq*., BPA has assessed whether potential environmental effects could result from adoption of the Policy, attached as Attachment 1 of this ROD.

As previously discussed in this ROD, the Policy—which would supersede the 2018 "Leverage Policy"[406]—is intended to provide guidance on capital financing decisions to optimize BPA's financial flexibility and ensure long-term consistency in its cost of service. To accomplish this, the Policy proposes revenue financing a portion of BPA's annual capital program and sets a debt-to-asset ratio target of no greater than 60 percent by the end of 2040 for both the business units and the agency.

Revenue financing collects funds through rates to finance a portion of capital investments, while a debt-to-asset-ratio (also known as leverage) is a financial indicator commonly used to measure the financial health of an entity and its ability to repay debt obligations. A high debt-to-asset ratio could negatively impact an entity's credit rating and interest rates. To achieve its enumerated debt-to-asset ratio targets by 2040, Section 5 of the Policy sets parameters for determining the amount of revenue financing for each rate period, but with flexibility to modify and re-purpose that amount based on certain circumstances.

The decision to adopt the Policy is thus primarily administrative and financial in nature and is not expected to result in reasonably foreseeable environmental impacts. Accordingly, BPA has determined that the decision to adopt the Policy does not require further consideration or documentation under NEPA at this time. To the extent that any future implementing actions for the Policy would have potential environmental effects, BPA will conduct any necessary NEPA reviews for such actions at that time.

6. CONCLUSION

For the reasons articulated above, the Administrator adopts the Sustainable Capital Financing Policy attached to this Record of Decision as Attachment 1.

Issued at Portland, Oregon, this 29 day of July, 2022.

JOHN HAIRSTON Digitally signed by JOHN HAIRSTON
Date: 2022.07.29 14:38:54 -07'00'

John L. Hairston
Administrator and Chief Executive Officer

[405] MSR Comments at 14 n.13; PNGC Comments at 1.

[406] The 2018 Leverage policy was aimed at managing Bonneville's debt-to-asset ratio by setting near-, mid-, and long-term business unit targets.

Attachment 1

Sustainable Capital Financing Policy

Sustainable Capital Financing Policy
July 2022

1. Background and Purpose

The Sustainable Capital Financing Policy (Policy) guides BPA's use of debt and revenue financing to finance its capital investments. Responsibly managing our outstanding debt, as well as controlling its growth in relation to the value of the underlying Federal assets, is vital to ensuring the sustained financial strength and viability of the Federal Columbia River Power System (FCRPS) for BPA's customers and their communities, and will help to ensure a more consistent cost of service over time.

BPA has a large capital program, generally spending between $500 million to $1 billion per year to reinvest in aging infrastructure and expand the existing system and capabilities. Over the years, the vast majority of the program has been funded with debt, which is not a common utility practice. It is common for some funding of the current capital program to come from current rates. Power has relied almost entirely on debt, primarily U.S. Treasury bonds with smaller amounts coming from the one-time Power Prepay Program and Congressional appropriations to the U.S. Army Corps of Engineers and Bureau of Reclamation. Transmission also relied on U.S. Treasury bonds, although a significant amount of investment was also funded through the lease-purchase program. Transmission also has investments built to meet the needs of specific customers who also finance the construction. These investments are generally described as Projects Funded in Advance (PFIA) and are liabilities BPA must repay with interest.

BPA's use of debt has a significant impact on its long-term financial strength and flexibility. High debt levels increase BPA's future fixed costs (interest expense), which will either increase rates or require BPA to reduce costs in other areas of the business to maintain the same level of total costs despite higher fixed costs. Further, debt levels have a direct impact on debt-to-asset ratios. A high ratio hampers BPA's ability to respond in times of financial stress and volatility by limiting its financial flexibility. Limited flexibility in times of financial stress or volatility can result in an unstable cost of BPA service. Furthermore, an entity's debt ratio, along with liquidity position and debt-service coverage ratio, is a key financial indicator. A high ratio, while one of many factors considered, could negatively impact BPA's credit ratings, which can result in higher interest rates.

This Policy establishes a predictable and consistent approach for determining amounts of revenue financing each rate period that is anchored to achieving our long-term debt-to-asset ratio target. Revenue financing will reduce BPA's use of debt, which will reduce future fixed costs, allowing for financial flexibility and a more stable cost of service over time. However, the revenue financing amounts are limited and debt will still play a major role in financing BPA's capital investments.

2. Definitions

Revenue financing: Raising funds through rates to recover the cost of directly paying for capital investments. In lieu of directly paying capital investments, funds could also be used to repay existing debt above the scheduled amounts if conditions warrant, such as to achieve greater interest savings by paying off existing debt rather than avoiding new debt.

BPA-funded capital investments: The portion of the BPA's total capital program that it would fund with debt (bonds, appropriations, lease purchase or power prepay), financial reserves, or revenue financing. It excludes commercial, customer-funded projects, which are generally categorized as PFIA, including those funded through Large Generator Interconnection Agreements (LGIA), Small Generator Interconnection Agreements (SGIA), and Line Load Interconnection Protocols (LLIP).

3. Scope

The Policy affects BPA's use of debt to finance the capital investment program for each individual business unit. It is intended to provide a consistent, long-term framework within which BPA can manage its capital funding practices.

4. Goals

The Policy goals are to establish a capital financing method that:

1. Moves BPA away from 100% debt financing by revenue financing a portion of capital, and
2. Achieves agency and business unit debt-to-asset ratios of no greater than 60% by 2040.

5. Policy

The default amount of revenue financing will be calculated for each business unit prior to each rate case as follows:

3. The default amount of revenue financing for each business unit will be 10% of the Integrated Program Review[407] loaded capital spending forecast of BPA-funded capital investments that are functionalized to each business unit.
4. However, if 10% revenue financing in step 1 results in a business unit debt-to-asset ratio that is greater than 60% by 2040 on a forecast basis, the default amount of revenue financing for that business unit will be increased to the lower of:

   (a) 20% of the IPR capital spending forecast of BPA-funded capital investment, or

   (b) Incremental revenue financing (compared to the amount of revenue financing included in the prior rate case) of $15 million per year for Transmission Services or $25 million per year for Power Services.[408]

BPA may propose or adopt an amount of revenue financing for a given rate period that is greater than or less than the default amount, in response to circumstances including, but not limited to: changes in BPA's capital program, prior or forecast triggering of risk adjustment mechanisms, rate pressure, settlement, likelihood of achieving the debt-to-

[407] Or its successor.
[408] The amounts in subsection (b) are based on incremental rate impacts of approximately 1% for each business unit, on a net-cost basis, which considers savings from avoided interest expense.

asset ratio policy goal, or whether an amount of revenue financing greater or less than the default amount occurred in a prior rate period.

Such circumstances do not require BPA to deviate from the default amount of revenue financing. This Policy and accompanying Record of Decision will be relevant evidence in making such decisions.

6. Implementation

The Policy will be implemented each rate period. The Administrator retains the discretion to use revenue financing to support business-line liquidity needs. BPA will propose to retain, within its calculations for risk adjustment mechanisms such as the Power and Transmission Financial Reserves Policy (FRP) surcharges and cost recovery adjustment clause rate adjustments, the requirement to repurpose revenue financing to support business unit liquidity needs in lieu of, or to reduce the magnitude of, these rate-increasing risk adjustment mechanism amounts. Additionally, when a business unit's start-of-year reserves for risk are between 60 and 120 days cash on hand, BPA intends that revenue financing will be reduced to the extent that a business unit's end-of-year reserves for risk are expected to be lower than the start-of-year. The reduction is limited to the amount needed to retain the start-of-year reserves for risk.

7. Periodic Review

The intent of this Policy is to provide durable guidance on capital financing decisions for long-term debt management. BPA intends to periodically review this Policy to consider its progress toward achieving the goals set forth in Section 4, to ensure the Policy is operating effectively, and ensure the Policy continues to align with BPA's strategic direction. BPA will request stakeholder input as part of this review. BPA expects to review the Policy approximately every five years.

BPA will also monitor and annually report its progress toward meeting the Policy goals.

8. Calculations

The following calculations are pertinent to the Policy:

1. BPA will calculate debt-to-asset ratios using the following formula: (Federal debt + Nonfederal debt + Deferred borrowing)/(Net Utility Plant + Nonfederal generation)
2. BPA will use audited financial statements to calculate actual debt-to-asset ratios for the last complete fiscal year to serve as the starting point for the forecast for each business unit.
3. BPA will use revenue requirements to calculate forecast ratios for each business unit. When calculating forecast ratios, BPA will use its forecast of capital spending as a proxy for new Plant in Service (an input into the Net Utility Plant component of the above debt-to-asset ratio formula) and for new debt. This is because actuals include Construction Work in Progress (CWIP) in the Net Utility Plant calculation. If BPA used a forecast of when plant goes into service in the future, it could double-count investments that are currently in CWIP. In addition, actuals include deferred

borrowing as debt. If BPA used a forecast of new borrowing, it could double-count existing deferred borrowing.

4. BPA will use end-of-year actual reserves for risk compared to the start-of-year reserves for risk balances to determine whether revenue financing is to be repurposed to support business unit reserves for risk.

BONNEVILLE POWER ADMINISTRATION
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