Fitch Ratings-Austin-25 August 2017: Fitch Ratings has assigned a 'AA' rating to the following revenue refunding bonds issued by the Idaho Energy Resources Authority, Idaho (IERA) and secured by payments from the Bonneville Power Administration (Bonneville):

--Approximately $200 million transmission facilities revenue bonds (Bonneville Cooperation Project No. 1), series 2017, taxable.

The Rating Outlook is Negative.

The bonds are scheduled to price on Sept. 11, 2017, via negotiation. Bond proceeds will finance the acquisition costs of certain transmission facilities that will be owned by the Idaho Energy Resources Authority and leased to the Bonneville Power Administration (Bonneville) according to a lease-purchase agreement.

In addition, Fitch has also affirmed the 'AA' ratings on debt issued by Energy Northwest, WA (ENW); Port of Morrow, OR; and Lewis County Public Utility District, WA, which are similarly secured by payments from Bonneville:

--$838.5 million ENW Project 1 revenue bonds;
--$3.8 billion ENW Columbia Generating Station revenue bonds;
--$1.04 billion ENW Project 3 revenue bonds;
--$811.6 million Port of Morrow transmission facilities revenue bonds, series 2012, 2014, 2015 and 2016-1& 2016-2;
--$78.9 million Lewis County Public Utility District No. 1 Cowlitz Falls hydroelectric project revenue refunding bonds, series 2013.

Fitch has affirmed Bonneville's implied revenue obligations at 'AA'.

The Rating Outlook on all ratings is revised to Negative from Stable.

SECURITY

The IERA series 2017 bonds are payable from lease payments made to the IERA from Bonneville, which are an absolute and unconditional payment obligation. Bonneville's payments are made as an operating expense from the Bonneville Fund and are on parity with the Bonneville Fund's pledged payments to ENW bonds, the Lewis County PUD hydroelectric project bonds and Port of Morrow transmission facilities revenue bonds. These payments are all paid prior to Bonneville's payments on borrowings from the U.S. Treasury ($4.8 billion) and federal appropriations debt ($2.9 billion).

KEY RATING DRIVERS

DECLINING RESERVES: The Negative Outlook reflects the continued trend of cash balance declines in the power business line. The relatively moderate 5.4% power rate announced in July reflects increasing competitive pressures at Bonneville. The combined impact of these trends and Bonneville's high leverage position could result in a rating downgrade.
BONNEVILLE'S OBLIGATION SECURES BONDS: The ratings on the Idaho Energy Resources Authority bonds reflect the credit quality of Bonneville and its absolute and unconditional obligation to make payments for debt service. Bonneville's pledged revenues include its power (73%) and transmission (27%) business lines.

REGIONAL POWER AND TRANSMISSION SUPPLIER: Bonneville provides wholesale power to a population of more than 12 million in the Pacific Northwest through a resource portfolio consisting of low-cost hydropower and nuclear generation. Transmission services are provided to a similar six-state region but to a broader cast of utilities.

MEDIUM-TERM POWER SALES CONTRACTS: Bonneville sells wholesale power through take-and-pay power sales contracts with 125 preference customers and federal agencies that expire in 2028. If new contracts are not signed beyond 2028, revenues available to service Bonneville's debt obligation would be reduced. Bonneville's ability to offer competitively priced power supply will be a key factor during the extension of its power sales contracts.

HYDROELECTRIC DOMINANT POWER SUPPLY: Power supply needs are met through a fleet of 31 hydroelectric projects and one nuclear project. Bonneville's predominantly hydro-electric generation portfolio results in hydrology risk and a variable energy supply. Low market energy prices in the region are placing competitive pressure on Bonneville to keep rate increases as low as possible and have driven wholesale energy revenues lower.

LEVERAGE HIGH; MODEST DECLINE EXPECTED: Debt levels are high with Debt/FADS (funds available for debt service) of 11.7x in fiscal 2016. Planned capital spending is manageable but Bonneville plans to debt finance nearly all of its planned capital spending, providing no financial flexibility in the form of rate-funded capital.

RATING SENSITIVITIES

LOW CASH LEVELS: The Negative Outlook reflects the cumulative pressure of declining cash reserve levels combined with Bonneville Power Administration's high debt burden, rate pressures and the financial variability of net margins for a hydroelectric utility. Continued low reserve levels and higher leverage could prompt a rating downgrade.

CREDIT PROFILE

The Idaho Energy Resources Authority (IERA) is a state entity, created in 2005 to finance electric generation, transmission and distribution facilities on behalf of wholesale and retail participating utilities operating in the State of Idaho. All financed facilities are constructed and operated by the participating utilities.

IERA will issue separately secured debt for each specific project. The participating utilities for which IERA finances projects are not authorized to file for bankruptcy. Title for the assets financed will convey to the participating utility upon final payment of the bonds used to finance acquisition of the assets. Series 2017 proceeds will be used to purchase 12 construction transmission lines and various affiliated equipment and infrastructure.

IERA and Bonneville will sign a lease purchase agreement on Sept. 21, 2017. Lease payments from Bonneville are equal to debt service on the series 2017 bonds plus an administrative fee. Lease payments secure repayment of the series 2017 bonds. Bondholders do not have a mortgage interest in the bonds and are secured only by lease payments. Bonneville will make unconditional payments directly to the Trustee; IERA has assigned its rights to the lease revenues to the Trustee.
Bonneville is the largest of the regional federal power marketing agencies within the Department of Energy. Bonneville accounts for approximately 28% of the electricity consumed and 75% of the transmission infrastructure in the six-state northwest region. The majority of Bonneville's revenues are provided by power operations. Transmission revenues accounted for approximately 27% of operating revenues in fiscal 2016.

NEGATIVE OUTLOOK

Cash reserves play a key role in managing aspects of Bonneville's sizable hydro-electric generation fleet. In addition, robust cash levels could provide financial flexibility in light of Bonneville's high debt levels and increasing competitive pressures from low cost energy in the region. Given the estimated $11 million in power business line reserves for risk projected at year end fiscal 2017, and annual declines experienced in each of fiscals 2016 and 2017 of approximately $150 million, downward rating action is likely if this trend is not significantly reversed.

Hydro-electric generation requires market sales in some months and market purchases in other months to balance the load demands with actual energy output. Bonneville's risk of revenue variability is managed primarily through its power business line cash reserves although Bonneville also has a $750 million line of credit with the U.S. Department of Treasury. Transmission business line reserves, which are robust, could be used by the power business line on an interim basis although Bonneville's business strategy and rate setting intends to operate each business line as a self-supporting entity.

Bonneville's power business line reserves for risk declined sharply in fiscals 2016 and 2017 due to weaker than anticipated wholesale revenues, declines in preference customer and industrial customer firm loads and regional pressure to keep rates low in order to remain competitive to market alternatives post-2028. At the end of fiscal 2015, Bonneville had $845 million in unencumbered reserves, which consisted of $395 million power business line reserves and $450 million transmission business line. Power business line reserves (referred to as reserves available for risk) declined to $159 million at the end of fiscal 2016. Bonneville estimates that power reserves will end fiscal 2017 at a minimal $11 million.

Despite the low level of reserves, the cost recovery adjustment clause (CRAC) did not trigger for the upcoming fiscal 2018 year. The CRAC allows for an adjustment to rates if reserves fall below $0, but the CRAC is only permitted to recovery reserves back up to the $0 minimum threshold and no higher. Bonneville hopes to increase the CRAC minimum threshold in the 2020 rate proposal.

FINANCIAL RESERVE POLICY AND POWER RATE INCREASE ADOPTED

In July 2017, Bonneville released its final 2018 rate proposal that includes a 5.4% power rate increase and 0.7% transmission rate decrease effective Oct. 1, 2017. As part of the 2018 final rate proposal, Bonneville adopted a financial reserve policy, which has been in development since 2014. The financial reserve policy established a minimum threshold of 60 days reserves for risk at each business line, or $300 million for power and $100 million for transmission. The final power rate increase included funding of $20 million per year until the minimum $300 million threshold is reached (the $20 million accounts for 1% rate increase out of the total 5.4%).

The decision to fund the power reserve at this slow pace tempers its value, in Fitch's opinion, until Bonneville is in adherence with the reserve policy. Bonneville notes that better than expected financial performance could increase the reserves above the $20 million per year. Absent a notable increase in the power business line reserves, a rating downgrade is likely.

COMPETITIVE PRESSURES ON POWER BUSINESS LINE
Bonneville sells energy produced from 31 hydroelectric plants owned and operated by the U.S. Army Corps of Engineers or the U.S. Bureau of Reclamation. Bonneville has direct-funding agreements with both agencies to pay operating and capex. The direct funding of capital improvements allows Bonneville to direct decision making and prioritization of reinvestment in the hydroelectric fleet. Bonneville also markets energy from nonfederal projects, the largest of which is CGS. CGS is a 1,150 MW nuclear plant (approximately 10% of Bonneville's total power supply).

In recent years the competitive margin between Bonneville's power rates and market alternatives has compressed due to very low natural gas prices, increased generation from renewables, declining energy demands in the region and increasing costs at Bonneville. Bonneville's current power supply contracts expire in 2028. Fitch expects Bonneville to engage in a multi-year process with customers well prior to 2028 to negotiate the next power supply contracts. Most of Bonneville's 125 preference customers receive all of their power supply from Bonneville.

REGIONAL COOPERATION DEBT

Bonneville and ENW have agreed to a regional cooperation debt plan that extends the maturity of outstanding ENW debt (CGS and projects 1&3) and uses the revenues made available from lower debt service costs on those projects to prepay higher interest rate debt to the U.S. Treasury. Debt for projects 1&3 is being extended to 2028 and debt for CGS is being extended as far out as 2044. The project operating license expires in December 2043.

While this plan effectively accelerates payment of Bonneville's subordinate lien obligations by extending the senior ENW bond maturity, it makes available federal borrowing capacity and provides economic benefit to preference customers, who are the ultimate ratepayers that repay both types of debt. Even with the extensions, only 16% of Bonneville's non-federal debt matures after 2028, when existing power contracts terminate.

RATING NOT BASED ON DIRECT FEDERAL SUPPORT

Fitch's implied rating on Bonneville reflects the credit quality of Bonneville as a self-supporting entity. Bonneville's subordinate obligations to the U.S. Treasury offer a layer of structural support to the Port of Morrow, Lewis County PUD and ENW bonds (non-federal debt), in that Bonneville must defer payment to the Treasury if it has insufficient funds to meet its non-federal debt. This provision provides payment flexibility, but Fitch's rating reflects the expected timely repayment on all Bonneville's obligations.

A linkage with the federal government exists in governance by the DOE, DOE Secretary appointment of the Bonneville Administrator, discretionary congressional review of Bonneville's budget, and the banking and lending relationship with Treasury. Recent federal discussions regarding curtailment of federal agency budgets are not expected to materially impact Bonneville. Bonneville's budget is not discretionary and not tax-funded, removing any estimated tax revenue benefit provided by a potential curtailment of Bonneville's budget.

Contact:

Primary Analyst
Kathy Masterson
Senior Director
+1-512-215-3730
Fitch Ratings, Inc.
111 Congress Avenue, Suite 2010
Austin, TX 78701
particular insurer or guarantor, for a single annual fee. Such fees are expected to vary from US$10,000 to US$1,500,000 (or the applicable currency equivalent) per issue. In certain cases, Fitch will rate all or a number of issues issued by a particular issuer, or insured or guaranteed by a group of insurers, guarantors, other obligors, and underwriters for rating securities. Such fees generally vary from US$1,000 to US$750,000 (or the applicable currency equivalent) per issue or in the case of a given security or in a given jurisdiction.

Ratings are not a recommendation to buy, sell, or hold any security. Ratings do not comment on the adequacy of market price, the suitability of any security for a particular investor, or the tax-exempt nature or taxability of payments made in respect to any security. Fitch receives fees from issuers, insurers, guarantors, other obligors, and underwriters for rating securities. Such fees generally vary from US$1,000 to US$750,000 (or the applicable currency equivalent) per issue. In certain cases, Fitch will rate all or a number of issues issued by a particular issuer, or insured or guaranteed by a particular insurer or guarantor, for a single annual fee. Such fees are expected to vary from US$10,000 to US$1,500,000 (or the applicable currency equivalent) per issue.

ALL FITCH CREDIT RATINGS ARE SUBJECT TO CERTAIN LIMITATIONS AND DISCLAIMERS. PLEASE READ THESE LIMITATIONS AND DISCLAIMERS BY FOLLOWING THIS LINK: HTTPS://WWW.FITCHRATINGS.COM/UNDERSTANDINGCREDITRATINGS. IN ADDITION, RATING DEFINITIONS AND THE TERMS OF USE OF SUCH RATINGS ARE AVAILABLE ON THE AGENCY'S PUBLIC WEB SITE AT WWW.FITCHRATINGS.COM. PUBLISHED RATINGS, CRITERIA, AND METHODOLOGIES ARE AVAILABLE FROM THIS SITE AT ALL TIMES. FITCH'S CODE OF CONDUCT, CONFIDENTIALITY, CONFLICTS OF INTEREST, AFFILIATE FIREWALL, COMPLIANCE, AND OTHER RELEVANT POLICIES AND PROCEDURES ARE ALSO AVAILABLE FROM THE CODE OF CONDUCT SECTION OF THIS SITE. DIRECTORS AND SHAREHOLDERS RELEVANT INTERESTS ARE AVAILABLE AT HTTPS://WWW.FITCHRATINGS.COM/SITE/REGULATORY. FITCH MAY HAVE PROVIDED ANOTHER PERMISSIBLE SERVICE TO THE RATED ENTITY OR ITS RELATED THIRD PARTIES. DETAILS OF THIS SERVICE FOR RATINGS FOR WHICH THE LEAD ANALYST IS BASED IN AN EU-REGISTERED ENTITY ARE AVAILABLE IN THE ENTITY SUMMARY PAGE ON THIS ISSUE ON THE FITCH WEBSITE.

Copyright © 2017 by Fitch Ratings, Inc., Fitch Ratings Ltd. and its subsidiaries. 33 Whitehall Street, NY, NY 10004. Telephone: 1-800-753-4824, (212) 908-0500. Fax: (212) 480-4435. Reproduction or retransmission in whole or in part is prohibited except by permission. All rights reserved. In issuing and maintaining its ratings and in making other reports (including forecast information), Fitch relies on factual information it receives from issuers and underwriters and from other sources Fitch believes to be credible. Fitch conducts a reasonable investigation of the factual information relied upon by it in accordance with its ratings methodology, and obtains reasonable verification of that information from independent sources, to the extent such sources are available for a given security or in a given jurisdiction. The manner of Fitch’s factual investigation and the scope of the third-party verification it obtains will vary depending on the nature of the rated security and its issuer, the requirements and practices in the jurisdiction in which the rated security is offered and sold and/or the issuer is located, the availability and nature of relevant public information, access to the management of the issuer and its advisers, the availability of pre-existing third-party verifications such as audit reports, agreed-upon procedures letters, appraisals, actuarial reports, engineering reports, legal opinions and other reports provided by third parties, the availability of independent and competent third-party verification sources with respect to the particular security or in the particular jurisdiction of the issuer, and a variety of other factors. Users of Fitch’s ratings and reports should understand that neither an enhanced factual investigation nor any third-party verification can ensure that all of the information Fitch relies on in connection with a rating or a report will be accurate and complete. Ultimately, the issuer and its advisers are responsible for the accuracy of the information they provide to Fitch and to the market in offering documents and other reports. In issuing its ratings and its reports, Fitch must rely on the work of experts, including independent auditors with respect to financial statements and attorneys with respect to legal and tax matters. Further, ratings and forecasts of financial and other information are inherently forward-looking and embody assumptions and predictions about future events that by their nature cannot be verified as facts. As a result, despite any verification of current facts, ratings and forecasts can be affected by future events or conditions that were not anticipated at the time a rating or forecast was issued or affirmed. The information in this report is provided “as is” without any representation or warranty of any kind, and Fitch does not represent or warrant that the report or any of its contents will meet any of the requirements of a recipient of the report. A Fitch rating is an opinion as to the creditworthiness of a security. This opinion and reports made by Fitch are based on established criteria and methodologies that Fitch is continuously evaluating and updating. Therefore, ratings and reports are the collective work product of Fitch and no individual, or group of individuals, is solely responsible for a rating or a report. The rating does not address the risk of loss due to risks other than credit risk, unless such risk is specifically mentioned. Fitch is not engaged in the offer or sale of any security. All Fitch reports have shared authorship. Individuals identified in a Fitch report were involved in, but are not solely responsible for, the opinions stated therein. The individuals are named for contact purposes only. A report providing a Fitch rating is neither a prospectus nor a substitute for the information assembled, verified and presented to investors by the issuer and its agents in connection with the sale of the securities. Ratings may be changed or withdrawn at any time for any reason in the sole discretion of Fitch. Fitch does not provide investment advice of any sort. Ratings are not a recommendation to buy, sell, or hold any security. Ratings do not comment on the adequacy of market price, the suitability of any security for a particular investor, or the tax-exempt nature or taxability of payments made in respect to any security. Fitch receives fees from issuers, insurers, guarantors, other obligors, and underwriters for rating securities. Such fees generally vary from US$1,000 to US$750,000 (or the applicable currency equivalent) per issue. In certain cases, Fitch will rate all or a number of issues issued by a particular issuer, or insured or guaranteed by a particular insurer or guarantor, for a single annual fee. Such fees are expected to vary from US$10,000 to US$1,500,000 (or the applicable currency equivalent) per issue.
equivalent). The assignment, publication, or dissemination of a rating by Fitch shall not constitute a consent by Fitch to use its name as an expert in connection with any registration statement filed under the United States securities laws, the Financial Services and Markets Act of 2000 of the United Kingdom, or the securities laws of any particular jurisdiction. Due to the relative efficiency of electronic publishing and distribution, Fitch research may be available to electronic subscribers up to three days earlier than to print subscribers.

For Australia, New Zealand, Taiwan and South Korea only: Fitch Australia Pty Ltd holds an Australian financial services license (AFS license no. 337123) which authorizes it to provide credit ratings to wholesale clients only. Credit ratings information published by Fitch is not intended to be used by persons who are retail clients within the meaning of the Corporations Act 2001.