

Customer Pre-payment Options

What it does:

This option establishes a means by which customers can effect an accelerated payment of power purchases to meet BPA cash needs. This option is assumed to be just one of possibly many in the realm of prepayment or shaped payment of surcharges.

How does it work:

There are a number of similar funding mechanisms—from a fidelity bond to a standby letter of credit—where a utility provides borrowed funds to BPA to the use of utility cash reserves. There may be other financial arrangements that a utility might make that would have similar characteristics. All of these mechanisms would be put in place to enable BPA to receive power purchase payments on behalf of customers in a time effective manner. In the borrowing cases, funds would be provided by a financial institution but backed by BPA customers.

A *fidelity bond* could have the characteristics of revenue anticipation bonds, with either a requirement by the lender for a bond reserve fund or insured interest rates. Each utility that elected to use a fidelity bond would provide for its own arrangements. BPA would be paid from the surety available—up to the surcharge amounts yet to be paid and limits established

Similar to a fidelity bond would be a *standby letter of credit* or similar instrument. Again, BPA would be paid under the LOC upon presenting an obligation to the lender. It is expected, from the utility's perspective, that this obligation would be considered a junior lien and would not count towards a utility's parity debt limit.

For these types of options, the customer's borrowings to meet power purchase obligations, would be backed by a utility's surcharges, not by BPA.

There are numerous such mechanisms. The smaller utilities may have an investment banking relationship that could provide similar services.

Alternatively, customers may elect to prepay all or a portion of their expected surcharge to BPA directly, perhaps out of their own cash reserves. BPA would need to have assurance that customers would timely prepay when needed by BPA. Customers would be credited with the prepayment against future surcharge obligations. BPA is investigating what kinds of assurance, credit standards, and/or signed agreements it will need to in order to rely on this mechanism for setting rates.

When do we trigger it and how?

The fidelity bond/letter of credit or surcharge prepayment agreement would be put in place at the beginning of the rate period. The mechanisms would be available for payment if and when a BPA surcharge is put in place [and, proposed by the customers but not agreed to by BPA,

higher priority sources of funds have been exhausted] (BPA's note: *this is a topic that would need more discussion before BPA could agree jointly to put this forward as part of this mechanism*) and the utilities have not used other options to provide funds to BPA.

In terms of timing, there are two options for its use as a source of funds, depending on whether or not cash flow under net billing can be made available for BPA's September liquidity problem. If a means of paying EN costs other than net-billing can be implemented, then the use of the fidelity bond/standby letter of credit or other prepayment vehicle need not occur until September 30 just prior to BPA's payment to Treasury. If the EN net-billing arrangement continues, then the maximum cash flow to the BPA fund would occur simultaneously with the May billing—before net billing participant payments are diverted to Energy Northwest.

Whom do we have to have agreements with to use the tool?

Each utility, of course, would have to have an arrangement with a financial institution to set up the standby terms. In addition, each utility would need to have an agreement directly with BPA for shaped payments or prepayments. Creditworthiness of the customer would also need to be established if BPA did not receive remittances directly from lending institutions. BPA would have to agree that the arrangement met its needs for assurance of cash flow, along with provisions of a BPA agreement.

How much money does it give BPA by the end of September to help with the Treasury payment?

Assuming a September implementation, the maximum amount would be the remaining surcharges owed by the utilities, but because of the probable nature of the surcharge — as a percentage increase on rates—there should be some discounting of the expected yield from a surcharge to allow for changes in loads from projections. That is, if the remaining surcharge collections amount to \$200 million, this mechanism should be discounted to provide only for, say, a \$150 million yield. A prepayment in May by 15 customers could result in as much as \$100 million to \$120 million increase to cash reserves on September 30. This estimate is based on prepayment of May to December surcharge payments at the maximum \$400 million surcharge. Alternatively, a prepayment in September by 15 customers who typically conclude net billing early could result in a \$40 million to \$60 million increase to cash reserves on September 30 based on prepaying September to December surcharge payments in September.

How much does it cost to use?

The cost to use can vary from a low of the cost of interest insurance for a fidelity bond to a ¼ % charge for the unused portion of a standby letter of credit. The actual amount loaned would carry typical interest rates for anticipation notes.

Ease of Use

Once the setting up a fidelity bond/letter of credit has been accomplished, the mechanism is easy to use.

Who pays? How is the utility cost of this tool recovered?

Bonneville could provide a discount to the shaped payments or prepayments whether directly from the utility or through a third party.

What is the critical mass? How many entities/utilities have to participate to make this work?

The critical mass for this option should be combined with all other sources of prepayment, which this mechanism resembles. Absent any other major sources of funds, such as DOP, the desired total to be provided would determine the critical mass, which might consist of the few who provide the most revenues. BPA's largest customers will need to participate in order for such a mechanism to have much effect on rates.

As a matter of equity, the number of utilities might need to be increased to provide a political critical mass.

When will we know if we can use the tool? That is, will we know before the Initial Proposal or the Final Proposal?

Because of the complexity of the setup, we will not know before the initial proposal. However, it would be useful to have the basic setup in place for anticipated settlement negotiations to take place some time after the pre-hearing conference.

Challenges/Issues/Problems with the use of this tool and the plan to resolve these

The challenge to this tool is acceptance by utilities, particularly with respect to other pre-payment substitutes. Targeting larger utilities initially would likely be most effective.

Is the tool viable?

The tool is viable as a financial instrument, but acceptance by utility commissioners is more problematical. It will need to be explained and sold to utilities.

Next steps/Summary check list of things that need to be done to get the tool into place

- Explain option to preference customer managers and commissioners to gauge willingness to accept this tool as one arrow in a quiver.
- Further refine potential financial instruments, with financial-institutional personnel
- BPA prepare list of customers that would provide critical mass.
- BPA explore nature of prepayment agreement and level of assurance necessary.
- In conjunction with other pre-payment options, place a menu before managers and commissioners to gauge final acceptance of any or all.

Contacts/References:

Jane Towery, Bank of America, (206) 358-8991 via Rich Bresnahan
Alex Johnston, Bank of America, 206.358.8938

Monthly Cash Recovery from May Billing of the Mid-Year CRAC

What it does:

BPA would consider its procedures for billing for the May mid-year surcharge to distribute the bills before net billing commences with bills mailed in June. This would allow the mid-year surcharge for May usage from net billing participants to go to BPA rather than to Energy Northwest. This should allow for BPA to have more cash on-hand on September 30 and result in an increase to the Treasury Payment Probability.

A mid-year CRAC would be implemented based on parameters established based on early water year flow forecasts, allowing BPA to increase rates beginning with April usage. Cash flows to BPA would increase in the latter part of May as customers pay their bills for April usage and the surcharge. June bills, which would continue the surcharge, would be net billed thereby increasing amounts going to Energy Northwest under the net billing arrangements, so that these obligations are completed earlier in the year. Additional revenues between June and September would result in BPA having more cash on-hand on September 30 and result in an increase to the Treasury Payment Probability.

How does it work:

At present, funds for May sales are billed in June and paid to Energy Northwest in July. Under the net billing agreements, payments due to BPA power and transmission sales beginning in July are remitted to Energy Northwest by each of the net billing participants until their annual obligation is fulfilled. Once the participant's obligation is fulfilled, they remit their payments to BPA. By implementing the terms on the bills for the May mid-year surcharge by estimating and mailing bills in May, BPA would receive the funds for the May mid-year surcharge rather than being paid to Energy Northwest. This tool would not change the amount of total BPA revenues, nor would it change any participant's net billing obligation. It changes only the timing of the payments between BPA and Energy Northwest.

A mid-year CRAC would be implemented that would trigger on a basis that is defined in a separate paper dealing with this subject. Should the CRAC trigger, BPA would implement a process to increase their power rates for one year beginning in April. April usage would be billed at the higher rates in May, with payments to BPA in the latter part of May. Because most public utility power customers are net billing participants, sales billed in June are first paid directly to Energy Northwest until the participant's net billing obligation is fulfilled. If a mid-year CRAC increases BPA rates, the payments to Energy Northwest would be completed sooner than without the CRAC. Some participants will fulfill their obligation before September, thereby generating additional cash to BPA prior to the treasury payment on September 30.

When do we trigger it and how?

- May mid-year surcharge billing can be adopted either in conjunction with the mid-year CRAC or adopted independently. It appears that BPA can introduce this change with a modification to the GRSPs.
- The triggering mechanism of a mid-year CRAC is discussed in a separate paper.

Whom do we have to have agreements with to use the tool?

- BPA billing staff
- Energy NW should be informed, as it may affect their cash flow

How much money does it give BPA by the end of September to help with the Treasury payment?

- The mid-year CRAC could provide an increase in year-end BPA cash of up to \$24M

What does it cost to use? Dollar cost, political cost?

- The mid-year CRAC would have negligible implementation costs.

Ease of Use

- Would be easy to use.
- May billing may require some adjustments on the mid-year surcharge.

Who pays? How is the cost of using this tool recovered?

- Cost changes would be imperceptible.

Is there a discount to the customer if the money comes from the customer?

- Not applicable
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What is the critical mass? How many entities/utilities have to participate to make this work?

- This would need to be a universal agreement for the power rate proposal.

When will we know if we can use the tool? That is, will we know before the Initial Proposal or Final Proposal?

- As soon as agreement of parties is accomplished.
- Given the proximity of the Initial Proposal, we will know if we can use this tool after the Initial Proposal and before the Final Proposal

Challenges/Issues/Problems with the use of this tool and how do we plan to resolve these?

- Because each participant has a different share of each of the three projects, the payment streams to BPA and Energy Northwest is different for each participant. Each customer would be affected differently, and the change to BPA's cash flow would be dependent upon the rate level and each participant's loads and obligations.

Other Benefits to the use of this tool

- Increases in cash available to BPA on September 30 reduce the need for PNRR in rates

Bottom line: Is this tool viable?

- Yes, this is a viable tool

Next steps/Summary check list of things that need to be done to get the tool into place

- Need to discuss in the context of mid-year surcharge discussions

Authors/contacts

Ray Bliven

rdb@r-c-s-inc.com

360-737-3877

Linc Wolverton

lwolv@tds.net

360-263-3675

Change Energy Northwest Fiscal Year and Net Billing Agreements' "Contract Year"

What it does:

Through a definition change in the Net Billing Agreements (NBA) Energy Northwest would change its "Contract Year" from July 1 through June 30 to January 1 through December 31. EN would also change its fiscal year to reflect the same period. There would be no change in participants' monthly bills, just where they are sent to.

How does it work:

At present, funds begin flowing to the BPA Fund at a significantly higher level in September/October after the EN Net Billing obligations are completed. This timing exacerbates BPA's end of fiscal year cash flow problem since its U. S. Treasury payments must be made at the end of September. If EN's fiscal year and its Net Billing Agreements Contract Year were shifted as described above, most net billing participants would begin their payments to ENW in January instead of July and complete their net billing obligations by May thus increasing payments by these customers to BPA during the last four months of BPA's fiscal year (June through September) and the first three months of the new fiscal year—a period in which BPA has cash-flow concerns. For more information;

http://www.bpa.gov/Power/queue/rates/Questions_and_Answers/Range_of_Monthly_Cash_Flow_to_Energy_NorthwestRR.pdf

When do we trigger it and how?

- This is a one-time change and requires a definition change in the NBAs by each of the 100 participants of the three projects.

Whom do we have to have agreements with to use the tool?

- Net Billing Agreement participants
- Energy NW
- BPA

How much money does it give BPA by the end of September to help with the Treasury payment?

- The benefit appears mostly in the first quarter of BPA's fiscal year—that is October through December. Relieves the \$100 million working capital assumption down to the \$20 to \$30 million level.
- Adoption of this tool would provide a better match of BPA's cash flow needs to net billing.

What does it cost to use? Dollar cost, political cost?

- EN staff has indicated that audit costs would increase by \$100 to \$200 k due to movement of the audit to the high demand time of year for auditors.
- Administrative and legal costs of changes to resolutions/agreements
- EN board members have indicated willingness to help on risk mitigation

Ease of Use

- Unanimous action by all participants needed, but once agreements are in place, nothing more needs to be done except utilities' and BPA changing where remittances are made.

Who pays? How is the cost of using this tool recovered?

- Administrative, audit and legal costs of revising agreements recovered through rates

Is there a discount to the customer if the money comes from the customer?

- Not applicable

What is the critical mass? How many entities/utilities have to participate to make this work

- Unanimous action required of participants
- EN board approval required
- BPA general counsel agreement needed

When will we know if we can use the tool? That is, will we know before the Initial Proposal or Final Proposal?

- Need to discuss with 100 participants
- Need to discuss with ENW board and members
- Most likely we will know if we can use this tool after the Initial Proposal and before the Final Proposal

Challenges/Issues/Problems with the use of this tool and how do we plan to resolve these?

- Over 100 participant utilities would have to sign for each of the projects they are in. NBAs would have to be amended, with related legal review and approval by customers' boards
- BPA cash balances would be lower during the middle part of its fiscal year than is currently the case, exposing BPA to higher amounts of non-deferrable costs in bad water/bad market years [I'm not sure this is true. Accumulations in the fall should be available throughout the winter.]
- Increased audit costs
- Bondholders may view this change unfavorably

Other Benefits to the use of this tool

- Improves benchmarking for EN, since EN would use the same calendar year as other utilities with whom EN benchmarks to improve operations and cost control.
- Would make EN's budgeting and cost control cycle better fit its business flow.

Bottom line: Is this tool viable?

- Yes, this is a viable tool

Next steps/Summary check list of things that need to be done to get the tool into place

- Additional in-depth cash flow resolution performed by BPA
- Amend NBAs
- Obtain Bond Counsel opinions
- Meet with EN Board Members and prepare EN Board resolution for approval
- Amend NBA's with related legal review and approval by customer boards

Authors/contacts

Rob Sirvaitis	rsirvaitis@prmlp.com	503-679-7300
Geoff Carr	ghcarr@pacifier.com	503-233-5823
Rich Bresnahan/EN	rabresnahan@energy-northwest.com	509-372-5730