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Re: Bonneville Power Administration's Compliance with the Remand of the Ninth Circuit Court of Appeals in *Industrial Customers of Northwest Utilities, et al. v. Bonneville Power Administration*, 767 F.3d 912 (2014).

Introduction

Thank you for the opportunity to comment on how the Bonneville Power Administration (BPA) complies with the remand instructions it received from the Ninth Circuit Court of Appeals in *Industrial Customers of Northwest Utilities v. Bonneville Power Administration ("ICNU")*, 767 F.3d 912 (9th Cir. 2014). As you know, the Public Power Council (PPC) was among those who challenged BPA's contracts providing cash subsidies to the direct service industrial customers (DSIs), and has consistently argued that BPA has an obligation to recover the money it illegally paid under those contracts.

While PPC appreciates the opportunity to provide input on BPA's response to the Court's remand, ultimately, it is BPA's responsibility to faithfully comply with the remand by conducting a thorough and independent analysis of the potential avenues for recovery of its illegal payments to Alcoa. Upon the issuance of the draft Record of Decision (ROD), PPC will review BPA's analysis and provide comprehensive feedback regarding whether BPA's analysis comports with the law, the facts, and Court's remand instructions.

The objective of these comments is to call BPA's attention to the facts that must be part of BPA's analysis on remand, and that, when viewed in the context of *ICNU*, clearly support BPA pursuing recovery of the money it illegally paid to Alcoa under the Alcoa Amendment. BPA's analysis on remand must be limited to the facts presented in the *ICNU* administrative record. BPA cannot supplement the record with after-the-fact rationalizations or speculations, and its findings must be supported by substantial evidence in the record. *See* 16 U.S.C. § 839f(e)(2); *Burlington Truck Lines, Inc. v. U.S.*, 371 U.S. 156, 168-69 (1962); *Hernandez-Cruz v. Holder*, 651 F.3d 1094, 1109-10 (9th Cir. 2011).

To begin with, BPA should approach this remand with a different focus than in the previous two remands.[1] Instead of finding new ways to justify its long-standing resistance to recovering its illegal payments to Alcoa, BPA should embrace the notion that agencies are certainly permitted to recover funds they erroneously or illegally disbursed, unless Congress statutorily precluded them from doing so. The Court reiterated this in *ICNU*, stating that "[e]ven in the absence of a specific statutory cause of action, the Government by appropriate action can recover funds which its agents have wrongfully, erroneously, or illegally paid." *ICNU*, 767 F.3d at 923 (internal quotations and citation omitted). There is no statutory or contractual bar to recovering the money BPA illegally paid to Alcoa under the Alcoa Amendment. Therefore, BPA should focus its analysis on *how* it will seek to recover that money.

If BPA embraces the notion that it can and should recover its illegal payments to Alcoa, it will be less likely to distort its analysis by being too generous to Alcoa. BPA's lack of objectivity in the DSI Lookback ROD was not lost on the Court in *ICNU*, as it observed that BPA "was far too generous" in evaluating the merits of Alcoa's possible defenses to BPA's claims for recovery. *Id.* at 927. It also noted that BPA's prediction regarding the likely success of Alcoa's estoppel defense was "particularly dubious," and that BPA did not objectively evaluate the degree of risk of Alcoa's asserted counterclaim "so much as capitulate to Alcoa's threats." *Id*. at 927-29.

Specific Issues

With regard to the specific issues identified by the Court in *ICNU*, PPC offers the following comments.

1. **Remand to BPA "to provide a defensible estimate of the amount of the subsidy it provided to Alcoa under the Alcoa Amendment prior to its invalidation."**

BPA has calculated that under the Alcoa Amendment, Alcoa received $25,627,143.95. Although no one other than parties to the transaction is likely to have better information as to the amount of that transaction, BPA's calculation of the amount it illegally paid to Alcoa appears to be supported by the evidence BPA provided, and is consistent with calculations PPC performed based on the best information available to it. However, the $25.6 million is not the full extent of damages suffered by the preference customers as that principal amount does not include lost interest earnings. In addition to the principal amount BPA illegally paid to Alcoa under the Alcoa Amendment, BPA should examine and seek recovery of the cost that preference customers incurred from the lost interest earnings on that principal amount.

2. **Remand to BPA "to provide some analysis of whether Alcoa's claim of net underpayment has any fair chance of success."**

Alcoa presented in *ICNU* the same counterclaim it previously presented to BPA: had BPA sold it physical power instead providing cash payments, Alcoa would have paid the IP rate, which was lower than the market price Alcoa ultimately paid during the Block Contracts and the Alcoa

[1] *Pacific Northwest Generating Cooperative v. Bonneville Power Administration ("PNGC I")*, 550 F.3d 846 (9th Cir. 2008) and *Pacific Northwest Generating Cooperative v. Bonneville Power Administration ("PNGC II")*, 596 F.3d 1065 (9th Cir. 2010).

Amendment. Brief of Intervenor Alcoa Inc. at 42-45, *ICNU*, No. 11-71368 (9th Cir. Aug. 3, 2012), ECF No. 68. Therefore, Alcoa reasons that it was damaged because it paid "over $218 million *more* for power [on the market] than it would have paid had BPA simply sold Alcoa physical power at the statutory IP rate." *Id.* at 3. Alcoa's contention is without merit, and, as BPA itself has recognized, "Alcoa's purported claim that it has been underpaid by almost $200 million is dubious and not supported by the *PNGC* cases." DSI Lookback ROD at 5, Petitioners' Excerpts of Record ("E.R.") 9.[2]

A. Alcoa's potential counterclaims arising under the Block Contracts are barred.

All potential counterclaims against BPA arising under the Block Contracts – which account for most, if not all, of Alcoa's alleged "damages"[3] – are barred. *ICNU*, 767 F.3d at 927. In *ICNU*, Alcoa argued that the mutual damages waiver included in the Block Contracts is enforceable and severable, and not contrary to public policy. Brief of Intervenor Alcoa Inc. at 28-29, 39, *ICNU*, No. 11-71368 (9th Cir. Aug. 3, 2012), ECF No. 68. The Court agreed and upheld the validity of the damages waiver clause. *ICNU*, 767 F.3d at 925. Because it was a mutual damages waiver clause that provided for a bilateral waiver of retroactive damages, it protects BPA from Alcoa's potential claims under the Block Contracts in the same manner the Court held it protects Alcoa against BPA's collection claims. In upholding the enforceability of the damages waiver clause, the Court specifically noted that "the aluminum DSIs gave up their ability to sue BPA to recover any costs associated with purchasing power through other means if the [Block Contracts] were invalidated." *Id.* at 926.

B. Alcoa's potential counterclaims arising under the Alcoa Amendment are not supported by the law or the facts, and have no merit.

Alcoa's potential counterclaims against BPA arising under the Alcoa Amendment are not supported by the law or the facts in the record. In an effort to make out a potential counterclaim against BPA, Alcoa distorted the facts in *ICNU*. Alcoa argued that "[h]aving decided to serve Alcoa and the DSIs, BPA had an affirmative obligation to sell them power at the IP rate." Brief of Intervenor Alcoa Inc. at 42, *ICNU*, No. 11-71368 (9th Cir. Aug. 3, 2012), ECF No. 68 (citation omitted). It admitted that BPA declined to serve Alcoa physical power, which it argued equated to "BPA compell[ing] Alcoa to purchase power at market rates which greatly exceeded the IP rate," causing "damage to Alcoa (i.e. paying net rates exceeding the IP rate)." *Id.* at 45.

The Court has repeatedly held that "BPA is not *required* to sell physical power to the DSIs." *ICNU*, 767 F.3d at 918 (citation omitted). "[I]f BPA does sell [physical power] to DSIs, it must offer them the IP rate," but it has no obligation to sell at all. *Id.* (citation omitted). Thus, the fact that BPA *could have* offered Alcoa a contract for the sale of physical power is irrelevant because

[2] As noted above, in analyzing the facts on remand, BPA is limited to the *ICNU* administrative record. Therefore, all citations to the record in these comments are to the *ICNU* administrative record.

[3] Brief of Intervenor Alcoa Inc. at 35, *ICNU*, No. 11-71368 (9th Cir. Aug. 3, 2012), ECF No. 68; *see also ICNU*, 767 F.3d at 928-29. (Both explaining that of its $218 million claim for "damages," Alcoa attributes $26.1 million to the Alcoa Amendment.)

the record is clear that BPA deliberately *refused* to sell Alcoa physical power in order to avoid the risks associated with doing so.

The ROD on issues remanded to BPA in *PNGC I* and *PNGC II* expressly stated that "the Administrator had determined that no offer other than the one developed by BPA [offer for cash payments rather than physical power] was on the table, and no further options would be forthcoming." *ICNU* Administrative Record ("A.R.") 0042, E.R. 42. BPA had previously explained that it preferred to provide DSIs monetary payments "in lieu of physically delivering power" "in order to eliminate the market and default risks to BPA associated with a traditional 'take-or-pay' physical power sales contract." A.R. 0093, E.R. 84. With regard specifically to the Alcoa Amendment, BPA had explained that

> BPA's decision to monetize this transaction is based, in part, on a desire to avoid the risks associated with making the relatively large wholesale market power purchases BPA would be required to undertake, in a short period of time, to serve Alcoa's currently operating load, together with the uncertainty that Alcoa will continue operating at existing levels for the duration of the Amendment Period, given current economic conditions. Monetization will allow BPA to provide benefits to Alcoa (and obligate BPA to incur expenditures) only in the event Alcoa operates its smelter facility, thereby protecting BPA from making wholesale market purchases that could be both unnecessary in the event Alcoa does not operate, and more expensive than anticipated if actual market prices exceed BPA's current market forecast.

A.R. 0308, E.R. 93; *see also PNGC II*, 596 F.3d at 1082 (Court reciting BPA's assertion of the same risks associated with selling Alcoa physical power). Finally, the contract itself clearly documented that "BPA has determined that, during the period of [Alcoa] Amendment, in order to minimize the cost risks of supplying Industrial Firm Power, the Parties will monetize the physically delivered Industrial Firm Power sale obligation." A.R. 0317, E.R. 102.

Unfortunately for Alcoa, it lost the argument that BPA had an obligation to sell it physical power (at the inexpensive IP rate), *PNGC I*, 580 F.3d at 812, and it failed to secure a favorable power contract from an alternate supplier. Thus, the business reality Alcoa faced, in light of BPA's refusal to sell it physical power, was purchasing the power it needed at full market rates. Surely, Alcoa was aware of the risks associated with its freely chosen business strategy. After all, the risks of having to purchase expensive power on the market were the very risks that BPA explicitly refused to take on.

In an effort to help the DSIs, and acting in what proved to be in excess of its statutory authority, BPA had initially offered to pay the DSIs $10/MWh for up to a total 500 aMW, but subsequently increased it to a $12/MWh for up to 577 aMW, which the DSIs could use to offset their cost of power purchases on the market. A.R. 3069, Intervenor Alcoa Inc.'s Excerpts of Record ("I.E.R.") 000107. Acknowledging that it "lacked other options" for acquiring power and noting that $12/MWh subsidy was "better" than $10/MWh subsidy, Alcoa was "willing to move forward with BPA in the development of contracts to implement the [offer made by BPA]." A.R. 3070, I.E.R. 000108. The fact that these illegal subsidies were not generous enough to cover Alcoa's market

purchases certainly does not entitle Alcoa to seek recovery of "damages," and any claim otherwise has no merit.

Finally, *PNGC I*, *PNGC II*, and *ICNU* foreclose the argument that the Alcoa Amendment was somehow functionally equivalent to a contract for the sale of physical power, and that once BPA agreed to provide "monetized service benefits," it agreed to "serve Alcoa and the DSIs." The Court made it clear that "an agency cannot expand its mandate solely through creative use of nomenclature" as BPA tried to do by calling the agreement to give money to the DSIs "a 'power sale' with 'monetized service benefits.'" *PNGC I*, 580 F.3d at 823; *PNGC II*, 596 F.3d at 1069 (citation to *PNGC I* omitted). In fact, when BPA tried to defend the Alcoa Amendment by asserting that the "*physical* sale of power to the DSIs has indirect benefits that might offset a below-market rate sale," the Court was quick to reject those arguments as "hav[ing] no direct application when, as here, BPA is not in fact physically selling power to the DSIs." *PNGC II*, 596 F.3d at 1074; *see also id.* at 1085 (noting that BPA's decision to sell physical power to Alcoa rather than provide cash payments "might produce a different result" on review). Thus, the Alcoa Amendment was a contract for BPA to provide Alcoa with up to $32 million in cash payments that increased the rates of BPA's preference customers, provided no direct benefit to BPA, subsidized the operations of BPA's competitors, and had no resemblance to a power sale. *See id.*

3. **Remand to BPA "to analyze alternative plans for recovery of any overpayment to Alcoa."**

While filing a collection claim against Alcoa is the most obvious path to recovery of BPA's illegal payments, it is not the only one. BPA itself has previously identified other potential avenues for recovery of the illegal payments (surcharge on future sales to Alcoa, *ICNU*, 767 F.3d at 921), and the Court has suggested that BPA should have evaluated other ways BPA might seek to recover the illegal payments, such as offsets from future sales contracts with Alcoa. *Id.* at 929. While we believe that, in light of *PNGC I*, *PNGC II*, and *ICNU*, BPA would be successful in prosecuting a collection action and securing a judgment against Alcoa, we encourage BPA to think creatively and carefully explore every possible avenue for recovery of the illegal payments.

4. **Remand to BPA "either to adopt one of those plans [for recovery of any overpayment to Alcoa] or to explain why, with respect to each of them, the costs and downside risks justify abandonment of the opportunity to recover any overpayment."**

To some extent, the Court answered this question when it rejected the rationales BPA offered for its decision to forego a collection action against Alcoa, which "boiled down to two: (1) Alcoa may have defenses to any equitable or quasi-contract claim, including perhaps an estoppel defense; and (2) Alcoa may be able to defeat a claim for unjust enrichment, and succeed on a counterclaim against BPA." *ICNU*, 767 F.3d at 927. The Court held "both rationales so implausible that they could not be ascribed to a difference in view or the product of agency expertise." *Id.* (internal quotation and citation omitted).

With regard to Alcoa's potential estoppel claims, the Court could not be clearer: "It is unlikely that the DSIs could successfully estop the government from recovering a refund if, in fact, a court determined that they had received unlawful overpayments." *Id.* Noting that BPA ignored

Supreme Court precedent reversing every finding of estoppel against the government with regard to monetary payments, and calling into doubt BPA's characterization of the Court as being "'more receptive to claims of estoppel against the Government,'" the Court stated that it "know[s] of *no* Ninth Circuit case estopping the government from recovering an erroneous monetary payment." *Id.* at 927-28. Thus, the Court concluded that "BPA's prediction that 'Alcoa would have a reasonably good chance of … mounting a viable estoppel defense against any claim by BPA,' is particularly dubious." *Id.* at 927.

The Court was not much kinder to BPA's legal analysis of a potential unjust enrichment claim against Alcoa. BPA has previously reasoned "that a claim for unjust enrichment cannot lie where the relationship between the parties is governed by a valid express contract concerning the particular issue." *Id.* at 928 (citation omitted). But the Court pointed out that by the time PPC and others challenged the DSI Lookback ROD, "this court had already invalidated the relevant portion of the Alcoa Amendment," and "[t]hat being so, no *valid* contractual provision stood in the way of an unjust enrichment claim." *Id.* (citation omitted).

The Court gave some slight credence to Alcoa's potential counterclaim, but only because the Court questioned whether BPA could "establish as a factual matter that it would have refused to sell Alcoa [physical] power at the IP rate" and whether Alcoa could establish that BPA likely would have sold it physical power. *Id.* at 929. Having raised this question, the Court immediately noted the "major flaw in Alcoa's argument, and BPA's acceptance of it as sufficiently meritorious to constitute a substantial risk in any litigation to recover, is that BPA could – under our *PNGC* decisions – have refused to sell Alcoa power at all, leaving Alcoa to buy power at full market rates." *Id.* In fact, as discussed above, that is precisely what happened. The record is clear that BPA repeatedly refused to sell Alcoa physical power. It refused to sell Alcoa power in order to avoid the risks of having to purchase expensive power on the market, and "the Administrator had determined that no offer other than the one developed by BPA was on the table, and no further options would be forthcoming." A.R. 0042, E.R. 42. Obviously, the Court was unaware of this evidence in the record when it wondered whether BPA could establish that it would have refused to sell Alcoa physical power.

Conclusion

Overall, *ICNU* provided substantial guidance for BPA to consider on remand. Given the guidance and analysis from the Court, BPA's focus must be on the fact that it can and should take action to make preference customers whole from the illegal payments it made to Alcoa. Although BPA must conduct a thorough and independent analysis, as described above, PPC believes the record is clear that BPA should seek recovery of the payments and lost interest earnings resulting from the illegal Alcoa Amendment. Additionally, Alcoa's potential counterclaims are unavailing from factual and legal perspectives. Thus, PPC looks forward to BPA's selection of a plan for recovery of its illegal payments to Alcoa.

Thank you for your consideration of these comments. Please do not hesitate to contact PPC for further clarification on any points.