BONNEVILLE POWER ADMINISTRATION RECORD OF DECISION RESPONDING TO THE U.S. COURT OF APPEALS FOR THE NINTH CIRCUIT'S REMAND ORDER TO BONNEVILLE OF CERTAIN ISSUES IN

Industrial Customers of Northwest Utilities, et al. v. Bonneville Power Administration, 767 F.3d 912 (2014)

I. INTRODUCTION

On September 18, 2014, the U.S. Court of Appeals for the Ninth Circuit issued *Industrial Customers of Northwest Utilities, et al. v. Bonneville Power Administration*, 767 F.3d 912 (9th Cir. 2014) ("*ICNU"*). *ICNU* is the third case in a series of related cases involving challenges to Bonneville's power sales contracts with its direct service industrial customers, primarily Alcoa, Inc. (Alcoa). In *ICNU*, the Court remanded to Bonneville to address four specific questions.

In response to the Court's remand order, Bonneville commenced this administrative process. On May 6, 2015, Bonneville issued a notice requesting public comment on the four issues identified by the Court. In light of the Court's finding that the record was inadequate to support Bonneville's conclusions with respect to the Alcoa Amendment, Bonneville requested commenters to provide any arguments they believed supported their respective positions that Bonneville should or should not pursue a recovery of benefits. A Draft Record of Decision (DROD) was issued on September 4, 2015, which responded to the questions posed by the court and comments made during the comment period. Interested parties were invited to provide comments on the DROD by October 9, 2015.

In its initial request for comments in May, Bonneville asked commenters to identify, in particular, any legal theories that could support a recovery of funds from Alcoa. Bonneville made this request to respond fully to the Court's remand and to provide an opportunity for commenters to help inform Bonneville's legal analysis prior to issuing the DROD. If there were any legal theories Bonneville may have previously overlooked, Bonneville wanted to find out what they were. However, no new legal theories were offered; therefore, BPA examined all bases for recovery that it believed might show some promise of obtaining a recovery in light of all of the circumstances surrounding this case.

In response to the DROD, PPC and PNGC have jointly provided the majority of detailed comments in support of the preference customers' position that BPA should reverse its earlier determinations and initiate recovery action.[1] PPC states:

> Rather than taking a fresh new look at the potential legal theories for recovery in the Draft ROD, BPA resigns to the fact that 'no new theories of relief were offered.' BPA does so despite the existence of a federal common law right and a statutory right to the government to recover the funds it erroneously or illegally

[1] NRU provided a more generalized statement, but urges Bonneville to adopt a legal analysis very similar to that proposed by PPC/PNGC. For ease of reference, Bonneville will refer to "PPC" when responding to PPC, PNGC and NRU.

> paid [citing *Old Republic,* discussed more fully below]. The Court in *ICNU* referred to both of these theories of recovery yet they are barely addressed in the Draft ROD.

PPC is correct that Bonneville stated "no theories of relief were offered." Bonneville made this statement because none were provided in support of the preference customers' perspective in the initial round of comments. However, the DROD did not, as argued by PPC, simply reiterate previous arguments or fail to take a "fresh look" at the issues under review. Instead, Bonneville thoroughly examined the legal theories that were the most relevant to assessing the issues identified by the Court and reaching a determination of whether initiating a legal process would be likely to lead to recovery of the amount at issue in this proceeding. Among other things, for instance, Bonneville reached the following conclusions for the first time in the DROD:

(a) Bonneville explained that there is a public policy exception to the common law rule that parties to illegal contracts are generally not entitled to a recovery of expended funds. Bonneville then explained why it believed the exception would not be likely to lead to a successful outcome were Bonneville to recommend that the government initiate a recovery action in this case. Previously, Bonneville had not identified or discussed this public policy exception, nor had it examined the general common law rule in as much depth.

(b) In the context of evaluating whether BPA has a viable claim of unjust enrichment against Alcoa, BPA concluded that a court would be likely to find that Alcoa had been "enriched." However, in light of the fact that Alcoa had done nothing improper to induce Bonneville to relinquish the contractual "benefit," it would be difficult to show that any enrichment was "unjust."

(c) Bonneville more fully evaluated the doctrine of mistake and found that Bonneville would be unlikely to prevail under a theory of mistake of law or fact.

(d) Bonneville found that Alcoa's arguments in favor of recovery lack any substantial degree of merit as an affirmative claim, in light of the Ninth Circuit's finding that Bonneville did not adequately consider the strength or weakness of Alcoa's potential claims against Bonneville. Bonneville also noted, without addressing the issue in detail, that Alcoa's arguments would likely be more persuasive, under the facts and circumstances here, as a defense, counterclaim, or rebuttal to the issue of damages. In light of the comments submitted in response to the DROD, additional discussion of that issue is undertaken elsewhere in this ROD.

See DROD, at 6 – 23.

PPC goes on to identify certain case law it believes Bonneville failed to consider as well as a statutory theory related to the collection of debts, and submitted a treatise on debt collection for Bonneville to review. Bonneville did evaluate a wide range of cases in the DROD and the original DSI Lookback ROD, including some of the cases now cited by PPC, and does not claim to have included every source that it consulted in preparing the DROD. Bonneville is also familiar with the Federal statutes governing debt collection, which were discussed to some extent in the DROD, and the policies of the U.S. Treasury with respect to debt collection.[2]

Nevertheless, Bonneville values the additional input and analysis provided by PPC and other interested parties. The ROD evaluates each of the additional authorities submitted by PPC in its comments to the DROD in the discussion below. In spite of the various paths of recovery identified in PPC's comments that are theoretically available to the Administrator, Bonneville does not believe that a viable pathway has been identified. To be clear, and as stated in the DROD, the purpose of the analysis is not simply one of identifying a potential cause of action that could conceivably form the basis for litigation to recover the money expended pursuant to the Alcoa Amendment. The purpose is to evaluate those potential theories and to come to a conclusion on the issue of whether, from a legal and business perspective, pursuing such a recovery is in the best interests of Bonneville and its customers. As discussed more fully below, the Administrator has concluded that it is not.

As discussed throughout this ROD, Bonneville concludes that there is significant risk that a claim against Alcoa could not be pursued successfully in court, and some possibility that Bonneville could end up in a worse position if it embarked on such a course. In such circumstances, Bonneville believes it is not prudent to recommend that the Department of Justice initiate litigation that will, in all probability, lead to unsatisfactory results.

From a business standpoint, the Administrator entered into the Alcoa Amendment to provide a bridge preserving the *status quo* until the Court's orders in *PNGC I* and *PNGC II* could be responded to more fully in public processes. Thereafter, the Administrator elected to continue negotiations for physical power sales contracts so as to preserve the business relationship with Alcoa if possible. Those new contracts were offered based on the Equivalent Benefits Test (EBT), a forecasting methodology that was developed in response to the Court's opinions to provide a basis for moving forward consistent with the Court's findings.

As it turns out, and as discussed more fully below, the Administrator's approach of continuing to contract with Alcoa subsequent to the issuance of *PNGC I* and *PNGC II*

[2] Alcoa also responded to the DROD with additional comments attempting to buttress its position that Bonneville should not attempt to recover the funds spent pursuant to the Alcoa Amendment. Those comments are also appreciated and have been considered, primarily in the context, as noted above, of assessing the merits of Alcoa's purported claims as defenses and counterclaims that could be posited in response to an affirmative action initiated by Bonneville. Alcoa also submitted untimely rebuttal in response to PPC citing case law and other materials that were not identified in PPC's initial comments. Bonneville has determined that the materials submitted in Alcoa's late response will not be considered as part of this proceeding.

was a sound business decision. Most importantly, Bonneville achieved far more net revenues by doing business with Alcoa rather than selling the same power in the open market due to market prices that turned out to be significantly lower even than those projected by the EBT forecast. Initiating collection and litigation activities would have placed those revenues at risk due to the substantial likelihood that Alcoa would not have been willing to both engage in an acrimonious collection dispute with Bonneville while at the same time negotiating future business transactions that would require paying an IP rate that was projected to significantly exceed market prices.

As it turned out, contracts between Alcoa and Bonneville in the wake of the *PNGC* decisions were highly beneficial to Bonneville from a financial perspective, far beyond the $25.6 million the Administrator expended pursuant to the Amendment. It should be recognized, as well, Bonneville believes that this continuing course of dealing between Alcoa and Bonneville would not be ignored in any legal proceeding initiated for the purpose of seeking repayment of the $25.6 million because it would go directly to the issue of the equities and intent of the parties. Simply put, it is highly unlikely that a court evaluating the facts and circumstances here would allow Bonneville to obtain all the benefits of these transactions without acknowledging that some of the equities in this case fall on Alcoa's side of the ledger.

II. BACKGROUND

PNGC I – The Block Sale Contracts

In 2006, Bonneville entered into five year power sales contracts with Alcoa and Columbia Falls Aluminum Company (CFAC), two aluminum smelting direct service industrial customers (DSIs), for service from 2007-2011. These contracts are generally referred to as the Block Sales Contracts. Under the Block Sales Contracts, the parties agreed that, for the first three years of service, in lieu of selling physical power to the DSI at the Industrial Firm Power (IP) rate, Bonneville would "monetize" these power benefits in the form of financial payments up to a pre-established cost cap. The Block Sales Contracts also gave the DSI the option of locking in the financial benefits for the entire five-year period if the DSI purchased a five-year block of power in the market.
Alcoa and CFAC elected to exercise this contractual option and provided documentation to substantiate their purchases in accordance with the terms of the contract.

In addition, Bonneville provided power to its only non-aluminum DSI, the Port Townsend Paper Corporation, through an arrangement with Port Townsend's public utility provider, Clallam PUD. Under this arrangement, Bonneville sold power at the priority firm (PF) rate to Clallam PUD, which then resold the power to Port Townsend.

The Block Sales Contracts and Port Townsend Contract were challenged by Bonneville's preference customers, the Industrial Customers of Northwest Utilities (ICNU), and Alcoa in *Pacific Northwest Generating Cooperative, et al. v. Bonneville Power Administration*, 550 F.3d 846 (9th Cir. 2008) ("*PNGC I*"). In *PNGC I*, the court found that, (1)

Bonneville has the discretionary authority, but not an obligation, to sell power to the DSIs; (2) if Bonneville chooses to sell power to the DSIs, it must first offer industrial firm power at the IP rate before offering any other form of power at a price other than the IP rate; and (3) the sale, as structured, did not comport with sound business principles. The court held that, although Bonneville has the authority to monetize its power sales contracts, its decision with respect to the Block Sales Contracts failed to satisfy its statutory obligation to provide the "lowest possible rates to consumers consistent with sound business principles." *PNGC I*, 550 F.3d at 875. The court made similar findings with respect to the Port Townsend Contract. In terms of relief, the Court did not invalidate the contracts or render them void. Instead, it remanded to Bonneville for a determination of the construction, applicability, and effect of the severability and damage waiver provisions that were part of the Block Sales Contracts.

PNGC II – The Alcoa Amendment

In response to *PNGC I*, Bonneville suspended service under the Block Sales Contracts to consider near term responses to the Court's remand. Within a few weeks, Alcoa and Bonneville entered into a twelve-month amendatory agreement (the Alcoa Amendment). The purpose of the Alcoa Amendment was to establish a short-term solution that would allow Alcoa to continue operations without disruption while Bonneville conducted a longer term administrative process to respond to the court's remand. The Alcoa Amendment provided that Bonneville would continue to provide Alcoa with monetary benefits during this interim period, but that such benefits would be calculated based on the IP rate.

Bonneville's preference customers and ICNU challenged the Alcoa Amendment as suffering from the same defects identified by the court in *PNGC I*. The court agreed, and in *Pacific Northwest Generating Cooperative, et al. v. Bonneville*, 596 F.3d 1065 (9th Cir. 2010) ("*PNGC II"*), remanded to Bonneville to determine whether and how it would seek recovery of the benefits provided to Alcoa under the Alcoa Amendment. Upon issuance of the Court's opinion, Bonneville suspended payments to Alcoa under the Amendment, three months prior to the expiration date.

The PNGC I & II Remands

In June 2009, Bonneville issued a letter to the region stating that it would begin an administrative process, referred to as the "Lookback," to address the issues remanded in *PNGC I* and *II*. On February 18, 2011, Bonneville issued its final record of decision ("Lookback ROD") on the remands in *PNGC I* and *II*. In the Lookback ROD, Bonneville decided that it would not pursue a recovery of funds from the DSIs.

As to the Block Sales Contracts, Bonneville concluded that the damage waiver provision was valid and enforceable, thereby precluding Bonneville from seeking a recovery. Bonneville also determined that, even if the damage waiver provision could not be enforced, there was no legal or equitable basis for recovery of the payments under the contract that had a reasonable chance of succeeding. Bonneville's analysis included a

limited discussion of Alcoa's purported claim against Bonneville but did not reach a definite conclusion regarding its merits. Bonneville did conclude, however, that it was reasonable to believe that if Bonneville initiated legal action, Alcoa would respond with a counter-claim as described in Alcoa's comments.

As to the Alcoa Amendment, Bonneville found that, even though it did not include a damage waiver, Bonneville had no legal or equitable basis for pursuing a claim against Alcoa that had a reasonable likelihood of success. Bonneville found, as with the Block Sale period, that if Bonneville did attempt to recover funds from Alcoa, Alcoa would most likely counter-claim against Bonneville for its alleged damages, which on its face could substantially exceed Bonneville's claim against Alcoa. Therefore, Bonneville determined that it would be unlikely to prevail in an action against Alcoa.

The ICNU Remand

In *ICNU*, Bonneville's preference customers and ICNU challenged Bonneville's decisions in the Lookback ROD, alleging Bonneville had constitutional, statutory and contractual obligations to seek a recovery of funds under all the challenged contracts. The Court upheld Bonneville's determinations with respect to the Block Sales Contracts and the Port Townsend contracts, but found that Bonneville's decision with respect to the Alcoa Amendment was not supported by the record.

The Court remanded the Alcoa Amendment and directed Bonneville:

(1) "to provide a defensible estimate of the amount of the subsidy it provided to Alcoa under the Alcoa Amendment prior to its invalidation;" *ICNU*, 767 F.3d at 929.

(2) "to provide some analysis of whether Alcoa's claim of net underpayment has any fair chance of success;" *Id.*

(3) "to analyze alternative plans for recovery of any overpayment to Alcoa; and," *Id.*

(4) "either adopt one of those plans or to explain why, with respect to each of them, the costs and downside risks justify abandonment of the opportunity to recover any overpayment." *Id.*

ICNU, 767 F.3d at 929.

III. SUMMARY OF COMMENTS

For the initial comment period that closed in June 2015, Bonneville received comments from seven parties. Five parties filed comments representing Bonneville's preference customer interests: Public Power Council (PPC), Pacific Northwest Generating

Cooperative (PNGC), Springfield Utility Board, Northwest Requirements Utilities (NRU), and Western Public Agencies Group (WPAG). Their comments are summarized below:

1. The commenters generally agreed that the amount identified by Bonneville of $25.6 M represented a fair and accurate assessment of the total costs incurred by Bonneville under the Alcoa Amendment, excluding alleged interest.

2. With respect to the issue of Alcoa's claim for net underpayment, commenters believe Alcoa's claim lacks merit and could not be sustained in an action against Bonneville.

3. As to the analysis of alternatives for Bonneville to seek recovery of the amount spent under the contract amendment, no new theories of relief were offered. These commenters asked Bonneville to take a more careful and probing look at the issue and to be creative in going about that task. Some suggested that Bonneville should find a basis for administrative offsets against Alcoa's current power purchase agreement.

4. Based on their analysis of the first three issues, these commenters urge the Administrator to attempt to recover the funds expended under the Alcoa Amendment.

In contrast to the comments from the preference customer community, Alcoa urged Bonneville to take no action to recover the funds. Alcoa stated that unjust enrichment was the only legal theory that Bonneville could possibly rely on and that such a claim would ultimately fail. Alcoa further argued that any type of administrative offset would be illogical and illegal. Alcoa also argued extensively that its claim of underpayment has merit and could be successfully prosecuted. Procedurally, Alcoa argued that dispute resolution is a matter covered by the terms of the Alcoa Amendment and must be followed if Bonneville proceeds with a recovery action, and that its claims would be pursued under the Contract Disputes Act and ultimately resolved in the Court of Federal Claims. Finally, there was one comment by Charles Pace that noted BPA deference and the difficulties of obtaining a recovery.

In response to issuance of the DROD, comments were provided jointly by PNGC and PPC adding more specific support for their original position. General comments in support of those views were provided by NRU. Alcoa provided detailed comments in support of its view and these too essentially expanded on points made earlier. Both PPC's comments and Alcoa's comments are addressed in this ROD.

IV. ANALYSIS OF ISSUES PRESENTED ON REMAND

Estimate of Amendment Payments

As presented in the Letter to the Region dated May 6, 2015, Bonneville's conclusion in the DROD was that it provided $25,627,143.95 in payments to Alcoa pursuant to the Amendment. Alcoa disagrees with the Court's characterization of these payments as a "subsidy" and notes that its own calculation "differs slightly" from the sum calculated by Bonneville. Alcoa Initial Comments at 2, n.3.

The PPC states that this sum appears consistent with its own calculations, but that it "does not represent the full extent of damages suffered by the preference customers as that principal amount does not include lost interest earnings." PPC Initial Comments at 2. However, Bonneville does not interpret the Court's directives as instructing Bonneville to provide an estimate of the preference customers' alleged damages. Rather, the Court asked Bonneville to provide "a defensible estimate of the amount of the subsidy it provided to Alcoa under the Alcoa Amendment prior to its invalidation." By directing Bonneville to calculate "the amount of the subsidy" and limit its estimate to the timeframe "prior to its invalidation," Bonneville believes the Court directed Bonneville to determine the total dollar amount Bonneville expended under the Amendment. Therefore, Bonneville has not revised its estimate to account for alleged post-termination interest expense.

In response to the DROD, commenters have registered no significant disagreement with Bonneville's determination that the amount of payments to Alcoa was approximately $25.6 million. Bonneville has reviewed its calculation and believes it is accurate. The Administrator finds that the defensible estimate requested by the Court is the sum identified in the May 6, 2015 letter -- $25,627,143.95. For purposes of convenience, Bonneville will refer to this amount as $25.6 million.

Alternative Plans For Recovery of Overpayment to Alcoa

A. <u>Introduction</u>

As a result of the Court's directives in *ICNU*, and after considering both rounds of public comments, Bonneville has reviewed the following avenues that could potentially lead to recovery of the funds BPA expended under the Amendment: (1) breach of contract; (2) contract illegality; (3) mistake of law; (4) unjust enrichment, and (5) administrative offset. Bonneville has also reviewed the Debt Collection Treatise submitted by the PPC. Each avenue is assessed to determine whether there is a reasonable probability of obtaining recovery of all or part of the $25.6 million.

In their comments, Bonneville's preference customers urged Bonneville to be creative in evaluating alternative paths for recovery and not restrict itself to traditional legal avenues.

PPC Initial Comments at 1-2. Their stated concern was that Bonneville provide a credible analysis that does not suffer the same faults as the analysis reviewed by the Court in *ICNU*. *See generally* PPC Initial Comments at 2. They cite various passages from *ICNU* and contend that, because their power rates include the costs incurred by Bonneville to serve Alcoa under the Alcoa Amendment, they have been injured and Bonneville must make every effort to recover these illegal subsidies. *See* PPC Initial Comments at 2-6.

As noted elsewhere, PPC and other representatives of the preference customers responded to the DROD by citing several authorities that had not been specifically discussed. While Bonneville's original analysis remains largely unchanged, Bonneville addresses the new material cited by PPC at this time.

In its opening comments, Alcoa argued that it is the party injured by the Alcoa Amendment. According to Alcoa, it suffered substantial losses related to its non-federal power costs incurred while under both the Block Sale Contracts and the Alcoa Amendment because Bonneville allegedly insisted on a monetized payment rather than offering a sale of physical power at the IP rate. Alcoa contended that if Bonneville had offered a physical power sale at the IP rate, Alcoa would have suffered none of the alleged losses. Alcoa further contends that, contrary to the arguments of the preference customers, Bonneville (and therefore the preference customers) has benefitted substantially from the Alcoa Amendment because it minimized Bonneville's costs, shifted the market risk to Alcoa at a time when the IP rate was below market prices, and has since resulted in Alcoa continuing to purchase power from Bonneville at an IP rate significantly above prevailing market prices.

In its response to the DROD, Alcoa fundamentally renews the same arguments and attempts to rebut, in several instances, Bonneville's perspective. This ROD attempts to summarize the primary points addressed by Alcoa but overall Bonneville's position remains unchanged: as an affirmative claim, Alcoa's position does not strike Bonneville as being particularly meritorious. However, in this ROD, Bonneville does acknowledge that Alcoa's position, whether as articulated in its comments or otherwise, does have weight when viewed as a defense to any claim that might be interposed as an affirmative claim by Bonneville. Seen in that light, the evaluation goes more toward how a court would be likely to balance the equities, as between the parties, were Bonneville to pursue litigation rather than viewing it through the lens of Alcoa initiating the prosecution of a claim for redress of a perceived injury.

Before turning to the analysis, it should be noted that settlement efforts were made to resolve this matter among the interested parties prior to commencing this formal administrative process. Shortly after the issuance of *ICNU*, representatives from Bonneville, Alcoa and public power met to discuss a potential resolution to the ongoing dispute regarding service to Alcoa and the recovery of funds. Representatives from Alcoa and the preference customers then met without Bonneville several times to attempt to reach a mutual resolution for presentation to Bonneville. Ultimately, these discussions were unsuccessful and did not lead to a resolution. Accordingly, Bonneville believes that

settlement or informal resolution is not a viable basis for resolution of the issues presented in the remand order.

B. <u>Potential Bases for Recovery</u>

1. Contract Issues

A breach of contract action can be successfully maintained if a party to the contract has failed to perform its material obligations. In this case, there is no dispute that both parties performed their obligations in accordance with the express contract terms. In short, Bonneville made the payments it was obligated to provide, and Alcoa purchased power from the wholesale power market at prevailing prices to maintain operation of its plants. Neither the preference customers nor Alcoa suggest that there has been a breach of contract by either Bonneville or Alcoa, or that a breach of contract theory provides a viable basis for a recovery of funds.

Further, no issue has been identified with respect to contract formation that could lead to recovery, nor does Bonneville believe that any such issues are present. Bonneville is authorized, but not statutorily required, to make contract offers to DSI customers. Thus, the Administrator's decision to do so is purely discretionary. Bonneville offered Alcoa a power supply arrangement that essentially hedged Bonneville's risk of having to acquire power from the market at what were expected to be high power prices and this approach achieved certainty with respect to Bonneville's financial risk. *See generally* Supplement to Administrator's Record of Decision on Bonneville Power Administration's Service to Direct Service Industrial (DSI) Customers for Fiscal Years 2007-2011. In return, Alcoa received a capped payment that partially offset its overall cost of power. However, the arrangement also meant that, by accepting Bonneville's offer, Alcoa incurred an obligation to manage and absorb the risk of price fluctuations, as it saw fit, in the wholesale power market. Ultimately, Alcoa accepted the offer.

The Administrator's final determination is that Bonneville has no viable basis for bringing an action based on a contract defect or breach of a performance obligation.

2. Contract illegality

a. As a general rule, contract illegality does not provide a basis for relief.

In *PNGC II*, the Court held that Bonneville's decision to monetize a power sale to Alcoa under the Alcoa Amendment exceeded Bonneville's statutory authority because it was not "consistent with sound business principles" as required by statute. *PNGC II*, 596 F.3d at 1069, 1080. The Court's determination that Bonneville exceeded its statutory authority, however, does not lead to the conclusion that Bonneville has a viable legal or equitable basis for obtaining a recovery of those funds.

The general rule under the common law is that neither party to an illegal contract is entitled to relief:

> [A] party to an illegal contract cannot ask the court to have his or her illegal objects carried out as the law will not aid either party to an illegal agreement. Rather, a court usually or typically will leave the parties where it finds them at the time the illegality is discovered, not restore the parties to the position they would have been in had the contract never existed.
>
> No action or recovery can be based on an illegal agreement either at law or in equity.

Am. Jur. at 297, 299.

This same general principle has been identified by *Williston on Contracts*:

> The effect of the rule that the courts will not aid either of the parties to an illegal transaction is that an executed illegal transaction, although based on an unenforceable bargain, is generally effectual between the parties.
>
> For instance, *one who has given illegal consideration or performed in whole or in part illegal acts specified in an agreement cannot recover reasonable compensation* or the stipulated price.
>
> *Money that has been paid for illegal services which have been rendered or in connection with a completed illegal transaction can generally not be reclaimed.* And where, because of illegality, money that would otherwise be owed cannot be recovered, the purported 'debt' cannot be raised by way of setoff.

Williston on Contracts, 19:78 (emphasis added).

Thus, the funds expended by Bonneville under the Alcoa Amendment are generally not recoverable on the basis that the contract was later held to be legally defective in some respects. Williston further explains that it makes no difference if the illegality results from an action taken in violation of statute: "[i]n denying relief to a participant in an illegal transaction, courts have noted that it is entirely immaterial that the defendant has been benefited if the agreement is of a seriously illegal nature *or is prohibited by statute*." *Williston On Contracts* (Fourth Edition), 19.74 (emphasis added); *see also* Am. Jur. at 297 (2d Ed.) .

b. The public policy exception to the general rule is not likely to be successful.

There is a limited "public policy" exception to the general rule that damages may not be recovered under an illegal agreement:

> In some instances a sound public policy may demand either the enforcement of an executory illegal agreement, or the rescission of an executed one such as when a denial of such relief by the courts would work a forfeiture disproportionate to the social interest supporting the public policy, or result in harm to those for whose protection such agreements are declared illegal. Thus, in some cases, public policy is best served by rescission or enforcement of the agreement, even though the result is to permit recovery by a guilty plaintiff, as, for example, if failure to rescind will affect not only the parties to the transaction but will injure the public. Accordingly, there are exceptions to the general rule that an executed transfer cannot be set aside, which may be included either under the head of an unexecuted illegal purpose or of parties not *in pari delicto*.

Williston at 19.75.

Based on this exception, an argument could be made that public policy would support Bonneville pursuing a recovery of funds against Alcoa. Because Bonneville's preference customers challenged the Administrator's decision to offer the Alcoa Amendment, they could arguably be considered "those for whose protection" *PNGC II* was issued. However, Bonneville does not believe it is likely that a court would find the argument compelling because there are competing public policy arguments that a court would necessarily need to weigh. For instance, it could be argued that recovery of the $25.6 million would serve the interests of public policy by directly reducing by $25.6 million the costs included in Bonneville's power rates. On the other hand, there are important policy interests served by upholding arm's length contracts that have been entered into by willing parties who materially rely on the Administrator honoring contractual obligations that he has agreed to.

In this case, it is undisputed that Alcoa fully performed its obligations under the Alcoa Amendment. It continued plant operations with power it purchased from the market in reliance on Bonneville's agreement to offset those costs with monetized power sales that provided a net power price more in line with the IP rate. This allowed Bonneville to avoid the risk of possibly acquiring power from a market subject to fluctuating prices to serve Alcoa. To require Alcoa to disgorge the benefit of its bargain would mean that Bonneville would obtain the benefit that it bargained for *(i.e.*, avoidance of price risk if Bonneville were to provide power directly) without having to pay any value for it, and that Alcoa would obtain no benefit at all. Completely depriving one contracting party of the benefit of its bargain would not be consistent with public policy governing contracts with the Federal government.

In *Veridyne Corp. v. U.S.*, 83 Fed.Cl. 575 (2008), the Court stated that forfeiture is not an appropriate remedy, even in cases where the illegality is "palpable," between the government and the contractor:

> The court in *Amdahl* recited the well-established proposition that, "though a contract be unenforceable against the Government because not properly advertised, not authorized, or for some other reason, it is only fair and just that the

> Government pay for goods delivered or services rendered and accepted under it." This is so even where "an award is plainly or palpably illegal" and "made contrary to statutory or regulatory requirements." . . . . The case law, properly read, does not support [the] argument that the appropriate remedy for any contract that is void *ab initio* is forfeiture of monies already paid or the denial of recovery in *quantum meruit* or *quantum valeba[n]t*. . . . Defendant has not pointed to any binding case law establishing that, absent a showing of bribe or a conflict of interest, voiding [the contract] *ab initio* would entitle the Government to forfeiture of all monies paid . . . for services already performed by plaintiff. Thus, absent the required nexus to bribery or conflict of interest, plaintiff would not be liable for the . . . forfeiture of all monies paid under [the contract] . . . .

Id. at 586 (citation omitted).

Veridyne suggests that it would be necessary to show some egregious conduct such as accepting a bribe or a conflict of interest on the part of the government to successfully invoke an exception that would support forfeiture of a contract payment. That is not the case here; there was no malfeasance or other unethical conduct, let alone bribery or conflict of interest. *See also John Reiner & Co. v. U.S.*, 163 Ct.Cl. 382, 325 F.2d 438 (1963) (a contract should only be nullified in the event that the illegality is plain on its face).

On the contrary, at the time the Alcoa Amendment was entered into, Bonneville believed, albeit mistakenly, that its actions were consistent with *PNGC I.* Bonneville took this position by tying monetization to the IP rate, as suggested by *PNGC I*, which explicitly did not prohibit monetization as a general matter. Moreover, the Amendment was never intended as a long term fix to the problem identified by the Court, but as a stop gap designed to preserve the status quo temporarily.

Additionally, a court weighing public policy might also consider that administrative law claims do not provide a basis for monetary relief and recognize that, in response to *PNGC I* an*d II*, BPA ultimately took other actions, consistent with the Court's opinions, to remediate the concerns raised in *PNGC II.* In particular, a court might consider that Bonneville developed the Equivalent Benefits Test (EBT), an economic forecasting tool, to guide the Administrator's future determinations of whether an offer of power service to a DSI customer is consistent with sound business principles. For that reason, a court might find that public policy does not require that Bonneville's preference customers receive a monetary remedy in addition to the administrative remedy that has already been obtained.

In the final analysis, there are competing public policy considerations that a court could consider in determining whether Bonneville is entitled to recover payments made pursuant to the Alcoa Amendment. However, Bonneville's final determination is that a court would not be likely to invoke this limited public policy exception and would, in all likelihood, resolve this issue by reliance on the prevailing rule that the illegality present in the transaction does not entitle either party to relief.

3. *Mistake of law*

Because the Alcoa Amendment could be characterized as having been entered into based on a mistaken belief about controlling law, Bonneville examined the potential for recovery based on the equitable theory of mistake of law. As a general rule, there is no relief for such mistakes:

> That a plaintiff who wishes to enforce an illegal contract did not know at the time of making it that it was illegal is immaterial. A party cannot take advantage of his or her mistaken belief about the application of a new law to his or her contract, for it is a mistake of law purely, and the ignorance of the law does not excuse.

Am. Jur. 298.

There are occasions when the general rule is not strictly followed:

> [T]he Restatement Second of Contracts provides that a party has a claim in restitution for performance that he or she has rendered under or in return for a promise that is unenforceable on grounds of public policy if he or she was excusably ignorant of the facts or of legislation of a minor character, in the absence of which the promise would be enforceable.

Bonneville does not believe the Alcoa Amendment fits within this narrow exception. Based on the court's opinion in *PNGC II*, Bonneville cannot credibly argue that it was "excusably ignorant of the facts" that led to its decision to continue monetized power sales under the Alcoa Amendment. As noted above, Bonneville mistakenly interpreted *PNGC I* and believed it was acting in conformance with that case, but was not ignorant of any relevant facts.

While mutual mistake can sometimes form the basis for reformation of a contract, that is not usually the case. In *C & L Construction Co. v. U.S.*, 6 Cl.Ct. 791 (1984), the Claims Court recognized that, even though mutual mistake of law may be a basis for reformation, exceptions to the general rule are rare, saying in part that "[t]he legal basis of this general rule is that both parties are generally held to have knowledge of the laws and regulations affecting their business dealings." *Id.* at 798 (citation omitted).

In *C & L Construction*, reformation was not permitted where the government and its counter party had agreed to specific terms regarding price. Here, the terms of the contract were similarly specific. As noted, in exchange for payments at a capped cost in lieu of a physical power supply, Bonneville avoided the risk of changing market prices and set its rates based on the certainty provided by the cost cap. Both parties had "knowledge of the laws and regulations surrounding their business dealings" and essentially got what they bargained for. *Id.*

A similar result was reached in *Anita Foundations, Inc. v. ILGWU Nat. Retirement Fund*, 902 F.2d 185 (2nd Cir. 1990). There, the Court explained that where two parties enter

into an agreement based on an understanding of the law that may be subject to further judicial interpretations, such a mistake will not lead to reformation of the contract. In reaching this result, the Second Circuit cited to and relied on a case from the Ninth Circuit involving a mistaken statutory interpretation:

> The Fund contends that the parties entered into the settlement agreements here based upon a mutual mistake of law -a statutory interpretation that subsequently was rejected by the Ninth Circuit decision. According to the Fund, *Geltman* established that the law applicable at the time of the settlements was different from what the parties thought it to be. Under the circumstances revealed here, however, the mistake of law doctrine is inapplicable.
>
> Succinctly put, "a settlement payment, made when the law was uncertain, cannot be successfully attacked on the basis of any subsequent resolution of the uncertainty." *Moses-Ecco Co. v. Roscoe-Ajax Corp.,* 320 F.2d 685, 690 (D.C.Cir. 1963). This apposite statement is consistent with the established rule that a change in the law does not render an agreement void. . . . At the time of the settlements, section 4225(a) had not been subject to judicial interpretation and therefore the Fund was aware that the agreements were entered into on the basis of an uncertain premise. There is no indication that the parties intended to avoid the settlement if "one party got a better bargain than had been anticipated" simply because the settlement was based upon a matter in doubt. *Leasco Corp. v. Taussig,* 473 F.2d 777, 781 (2d Cir. 1972); *cf. Gerard v. Almouli,* 746 F.2d 936, 939 (2d Cir. 1984).

Anita Foundations, Inc. v. ILGWU Nat. Retirement Fund, 902 F.2d 185 (2nd Cir. 1990).

The facts surrounding the parties' agreement to the Alcoa Amendment are similar to the facts in *Anita Foundations*. The law surrounding DSI service was, in some respects, unsettled at the time the Alcoa Amendment was executed. Indeed, the opinion in *PNGC I* had just been released and the mandate had not even issued. The parties entered into the Alcoa Amendment based on an "uncertain premise" due to a mistaken "statutory interpretation that subsequently was rejected by the Ninth Circuit decision." As in *Anita Foundations*, the subsequent judicial interpretation in *PNGC II* demonstrated that the parties' understanding of the law at the time the contract was executed was incorrect. Regardless of whether *PNGC II* represented a change in law or a clarification of the existing law, under *Anita Foundations*, that change or clarification would not necessarily render the Alcoa Amendment subject to rescission. Thus, the doctrine of mistake of law would provide no viable avenue for restitution.

Further compounding the problems inherent in a mistake of law argument is the fact that existing law, including Federal case law, is even more unfriendly to claims of unilateral mistake of law than it is to claims of mutual mistake of law: "a unilateral mistake is not cause for the reformation of the contract." *Parker Beach Restoration, Inc. v. U.S.*, 58 Fed.Cl. 126(2003); *National Union Fire Ins. Co. of Pittsburgh, Pa. v. D & L Const. Co.*,

353 F.2d 169 (8th Cir. 1965); *Commercial Union Ins. Co. v Keebler Co*., not reported in F. Supp., 1990 WL 93324 (W.D. Ill. 1990).

In this case, Bonneville is the party charged with responsibility for interpreting the statutes that govern its activities. Therefore, it could be reasonably argued that any mistake of law was primarily due to Bonneville's mistake of law rather than the mutual mistake of Bonneville and Alcoa. A court, therefore, might well be persuaded that Bonneville was primarily responsible for the mistaken statutory interpretation, which would make Bonneville's likelihood of recovery even more attenuated.

In conclusion, Bonneville's final determination is that the doctrine of mistake of law would not provide a basis to recover funds expended under the Alcoa Amendment.

4. *Unjust Enrichment*

Lastly, BPA evaluated the potential for obtaining recovery based on a theory of unjust enrichment. The elements of an unjust enrichment claim are fairly straightforward:

> To succeed on a claim of restitution based on a theory of unjust enrichment, the Government must establish the following elements: "(1) a benefit conferred on the [plaintiff] ; (2) an appreciation or knowledge by the [plaintiff] of the benefit; and (3) the acceptance or retention by the [plaintiff] of the benefit under such circumstances as to make it inequitable for the [plaintiff] to retain the benefit without payment of its value." Richard A. Lord, *Williston on Contracts* § 68:5 (4th ed.); *Caroline Hunt Trust Estate v. United States,* 470 F.3d 1044, 1052 (Fed. Cir. 2006) (citing *Westfed Holdings, Inc. v. United States,* 407 F.3d 1352, 1370 (Fed. Cir. 2005)

International Air Response v. U.S., 75 Fed.Cl. 604 (2007); Restatement (Third), Sect. 1.

a) Was Alcoa enriched by the Amendment?

The first issue to be determined is whether a benefit has been conferred on another party. Most of the cases reviewed do not focus on this aspect of an unjust enrichment claim and are decided based on the third prong regarding whether the circumstances make retention of a benefit inequitable. Nonetheless, the party claiming restitution pursuant to a theory of unjust enrichment must prove that the other party was enriched. *Caroline Hunt Trust Estate v. United States,* 470 F.3d 1044, 1052 (Fed. Cir. 2006)

In this case, Bonneville provided payments to Alcoa of $25.6 million during the period when the Alcoa Amendment was in effect. The purpose of the payments was to offset the cost of power that Alcoa was required to purchase from the market as part of its contract with Bonneville. To that extent, Alcoa was benefitted by the contract payments.

However, Alcoa claims that during the period of the Alcoa Amendment it lost $34.5 million because it paid $60.5 million for market power, but only received $25.6 million

in monetary benefits from Bonneville. *Id*. at 19. Alcoa's argument finds some support in *ICNU*:

> The ROD's second rationale – that Alcoa may be able to show that it was not enriched, but rather illegally disadvantaged, by the subsidies in the Alcoa Amendment – has more support in the record. The record does establish, at least, that the amount of any damages BPA could actually recover from the aluminum DSIs is uncertain and disputed. Moreover, if BPA sues, Alcoa could well counterclaim, arguing that it actually lost money through the partially invalidated contracts.

ICNU, 767 F.3d at 928.

Nevertheless, Bonneville believes Alcoa made a decision to execute the Amendment because it was in Alcoa's business interests to do so even though Alcoa, like any business entity, may have preferred a better deal. Alcoa understood that Bonneville was no longer legally obligated to offer power service for its regional aluminum smelting operations. It also understood that Bonneville had an interest in maintaining a commercial relationship with Alcoa or it would not have been willing to offer the Amendment.

However, it was also clear that Bonneville was not willing, at that time, to offer a physical power sale. It is not clear if such an abrupt change to a physical power sale would have been particularly advantageous to Alcoa at the time of the Alcoa Amendment. In order to support a transaction of only nine months duration, Alcoa probably would have been required, on short notice, to make alternative arrangements for the power it had already purchased from the market under the Block Sale Contract. This is because Alcoa would not have been able to use that power to operate its plant if it were supplanted by a power supplied directly by Bonneville. Bonneville notes, however, that Alcoa disputes this assertion in it comments on the DROD and accepts that it remains a disputed issue. Alcoa DROD Comments at 13.

Nonetheless, Alcoa's realistic choices were either to accept Bonneville's offer of the Amendment and continue to receive an offsetting payment for its own purchased power, or operate with the power it had already purchased from the market at full price without the offset from Bonneville. The short term Alcoa Amendment was a reasonable, workable temporary solution for both Alcoa and Bonneville.

In this case, Alcoa made the perfectly reasonable choice to accept Bonneville's offer in order to offset the costs of its power purchases. Contrary to Alcoa's comments, that does not make it a "Hobson's choice" between two equally unpalatable alternatives. Alcoa Initial Comments at 5. The fact that Alcoa may have preferred more favorable contract terms, such as more money or physical power from Bonneville, does not mean it was not enriched by the benefits it received under the contract it elected to sign. In the absence of these payments, based on Alcoa's own argument, Alcoa's purchased power costs would

have been $60.5 million; with these payments, its costs were $34.5 million. In that sense, Alcoa was enriched in the amount of $25.6 million.

In comments, Alcoa disputes Bonneville's conclusion for a number of reasons. The reasons cited are largely conjectural and appear to be based primarily on Alcoa's assessment of its alleged damages, an issue dealt with more fully in other sections evaluating the merits of Alcoa's asserted claim against Bonneville. Alcoa DROD Comments at 13 – 15. Thus, Bonneville acknowledges Alcoa's position on this issue but sees little point in further evaluation in this section of the ROD, particularly in light of Bonneville's conclusion that it would be very unlikely to prevail on an unjust enrichment claim for separate reasons.

Bonneville's final determination is, for purposes of evaluating a claim for unjust enrichment, Alcoa was enriched by $25.6 million.

b) Did Alcoa appreciate and have knowledge of the benefit?

The second element of the undue enrichment test is whether Alcoa appreciated or had knowledge of the benefit it received. This element actually highlights, in part, why the doctrine of undue enrichment generally does not apply to cases involving express contracts. *Nichols v. Heslep*, 2001 WL 1066919, at *3 (5th Cir. Aug. 14, 2001). Under an express contract, a party invariably has knowledge of the benefit it receives because the benefit is set forth in the contract and is almost always a primary purpose of the contract. In this case, the benefits obtained and received in the Alcoa Amendment were embodied in the express contract terms that were the product of a negotiated arms-length agreement between sophisticated parties. As a result, Alcoa had full knowledge of the benefit it bargained for and received. This second prong of the three part test is readily satisfied.

c) Was the benefit accepted or retained by Alcoa under such circumstances as to make its retention inequitable?

The central issue in this case and in most cases involving claims of unjust enrichment is whether retention of the benefit is unjust. "Enrichment" in and of itself is not sufficient to support a finding of unjust enrichment. *Nichols v. Heslep*, 2001 WL 1066919 (5th Cir. 2001), succinctly summarizes the general principles found throughout case law:

> [W]here a person has "obtained a benefit from another by fraud, duress, or the taking of an undue advantage," he may recover based on a theory of unjust enrichment. *Heldenfels Bros. v. City of Corpus Christi,* 832 S.W.2d 39, 41 (Tex. 1992). However, unjust enrichment is not an appropriate remedy "merely because it might appear expedient or generally fair that some recompense be afforded an unfortunate loss to the claimant, or because benefits to the person sought to be charged amount to a windfall." *Id.* at 42 (internal quotations

> omitted); . . . . Furthermore, recovery for unjust enrichment is impermissible where the "same subject is covered by an express contract."

Id. (emphasis added) (internal citations omitted). *See also*, *Alvarado v. Microsoft Corp*., Slip op., 2010 WL 715455 (W.D. Washington 2010) ("it is critical that the enrichment be unjust as both under the circumstances and as between the two parties to the transaction").

In evaluating whether a party was enriched unjustly, the courts examine the relationship between the parties and look for some kind of behavior on the part of the person who has been enriched that would make retention of the benefit unjust. As noted above, courts generally look to see if there has been fraud, misrepresentation, duress, or other wrongful conduct on the part of the party receiving the benefit. The bottom line is that it is only unjust to retain a benefit if the party retaining it somehow induced the other party to relinquish it through some material impropriety.

In *Association Ben. Services, Inc. v. Caremark RX, Inc.*, 493 F.3d 841 (7th Cir. 2007), the Court explained that, in a similar case,

> Athey was required to prove that Harris unjustly retained a benefit to Athey's detriment, and that Harris' retention of that benefit violates fundamental principles of justice, equity, and good conscience. In the absence of clear and convincing evidence of fraud by Harris, we cannot say that Harris unjustly retained a benefit and was thus unjustly enriched. Athey's unjust enrichment claim was properly dismissed.

Id. at 855 (citing *Athey Products Corp. v. Harris Bank Roselle,* 89 F.3d 430, 436 (7th Cir. 1996). In *Nichols v. Heslep*, 273 F.3d 1098, 2001 WL 1066919 (5th Cir. 2001), the Court rejected a claim of unjust enrichment for similar reasons:

> The district court found that the Nichols' unjust enrichment claim fails as a matter of law because there was no evidence that the Hesleps obtained a benefit through fraud, duress, or undue advantage and because the subject matter of the dispute was governed by an express contract. . . . The Nichols cultivated and added improvements to the Hesleps' land because of their mistaken belief that the parties had an agreement, not because of fraud, duress, or undue advantage. Also . . . the existing contract between the parties was controlling and dictates that there be no recovery for the Nichols for unjust enrichment or any other theory under which they might have sought restitution.

Id. at 3.

In short, the Court found there was no viable claim for unjust enrichment because there was no evidence of fraud, duress, or undue advantage, and an express contract governing the relationship between the parties precluded recovery under an unjust enrichment theory. *See also Sullivan v. Leor Energy*, LLC, 600 F.3d 542, 30 IER Cases 867 (5th Cir. 2010); *Tupper v. Roan*, 349 Or. 211, 243 P.3d 50 (2010)("our unjust enrichment cases

speak of a range of circumstances that could be deemed wrongful, including mistake, fraud, coercion, undue influence, duress, taking advantage of weakness, and violation of a duty imposed by a confidential or fiduciary relationship.")

Here, there is no dispute that Alcoa did not engage in fraud, duress, or undue advantage to obtain the benefits of the Alcoa Amendment. Indeed, no party even alleges that such conduct has occurred. Thus, a claim for unjust enrichment would ultimately fail on that basis alone.

Further, the existence of an express contract – the Alcoa Amendment - and its role in the success of an unjust enrichment claim cannot be totally ignored. In *ICNU*, the Court found that the general rule precluding an unjust enrichment claim where there is an express contract may not be applicable because the payment provisions were invalidated. *ICNU*, 767 F.3d at 928. Even though the Court concluded that a partially invalidated contract may not preclude a claim for unjust enrichment, the terms of an express contract may still be relevant to determining whether a party was *unjustly* enriched under the circumstances. In that regard, there is authority that, in the context of unjust enrichment claims, the existence of an allocation of benefits agreed to by the parties is an important factor.

In *Monus v. Colorado Baseball 1993, Inc.,* 103 F.3d 145 (Table) (10th Cir. 1996), the Court found:

> Having received the benefit of the bargain he agreed to, plaintiff has made no showing that there are inequitable circumstances justifying his claim of unjust enrichment. We therefore reject his claim of unjust enrichment.
>
> FN6. We do not suggest that an unjust enrichment claim can permit recovery where, as here, there is an express contract which has been fully performed. We do not believe the unjust enrichment doctrine can be used to re-write contracts which one party alleges are "unfair," in the absence of evidence of fraud, duress, mistake, or the like.

See also Hogan v. Wright, 356 F.2d 595, 598 (6th Cir. 1966) ("Courts do not relieve a party competent to contract from an improvident agreement in the absence of fraud or bad faith").

Irrespective of the issue of partial invalidity, the Alcoa Amendment is an express agreement between the parties that clearly describes the benefits given and received by the parties. Although the existence of the express contract may not categorically preclude a claim of unjust enrichment in this instance, it nevertheless may further weaken or undermine Bonneville's ability to show that the enrichment was unjust.

In this case, Bonneville believes there is little, if any, basis for Bonneville to seek recovery based on unjust enrichment. There is no credible basis to argue that Alcoa engaged in wrongful conduct of any kind that would sustain such a claim. The Alcoa Amendment was the result of an arm's length negotiation between two sophisticated

parties with decades of experience contracting with each other in the normal course of business. Bonneville was not acting under duress, fraud, misrepresentation, inducement, or any other wrongful conduct on the part of Alcoa. Once the Amendment went into effect, Bonneville paid money to Alcoa that it agreed to pay, and Alcoa received the benefits it expected to receive. Alcoa fully performed its obligations under the contract, including purchasing higher cost physical power from the market. As a result, even though Bonneville believes that Alcoa was enriched under the contract, there is no basis to find that it was enriched unjustly.

The doctrine of unjust enrichment is based on the theory that the receiving party should disgorge the benefits because, as a matter of equity, it should not be enriched by its own transgressions. In this case, because there is no malfeasance or improper conduct by Alcoa, there is no equitable basis for finding that Alcoa should relinquish the benefits.

For these reasons, Bonneville's final determination is that it is not likely to prevail on a claim Alcoa was enriched unjustly.

5. *Administrative offset, rate adjustment, and common law setoff*

Alcoa's comments deal at length with potential means of recovering the $25.6 million paid under the Alcoa Amendment through various administrative actions. Alcoa concludes that none of these would be appropriate. Although Bonneville does not agree with all aspects of Alcoa's assessment, Bonneville concludes that administrative recovery or offset is not a viable path to recovery.

a) The Federal Claims Collection Act of 1966 (FCCA), as amended by the Debt Collection Act of 1982 (DCA), does not provide a viable avenue for recovery.

Alcoa posits several reasons why the FCCA and DCA are unavailable as tools to recover payments made under the Alcoa Amendment. Alcoa Initial Comments at 13. Alcoa argues that BPA cannot rely on the FCCA and DCA without following the dispute resolution terms appearing in the Alcoa Amendment and concludes that, without taking those steps, there is simply no debt to collect until the matter is contested through litigation and BPA obtains a judgment. *Id.* Alcoa asserts that the FCCA and DCA authorize agencies to "collect [a] claim by administrative offset" only after trying to collect that claim by other methods. *Id.* Alcoa further argues that the FCCA and DCA are inapplicable because the potential claims at issue here are subject to the Contract Disputes Act, which has its own independent procedures for recovery that are not available under the FCCA and the DCA. *Id.* at 15.

Alcoa also raises arguments about proper venue, jurisdiction and procedure which must be considered if Bonneville determined that it would, in fact, attempt to seek a recovery of funds from Alcoa. They are all directed towards identifying the path Bonneville would or should follow if it tried to recover these funds. Because Bonneville's final determination is that it will not be seeking such relief, regardless of the particular

pathway, it is not necessary to provide a detailed response to these jurisdictional arguments.

b) For practical reasons, significant offsets from future power sales are not likely to materialize.

Alcoa goes to great lengths to show that Bonneville would be unable to recover the payments by allocating the $25.6 million to the IP rate that is charged for industrial firm power. *Id*. at 15–16. Alcoa believes that the statutory rate directives that would be relevant to such a determination preclude such a cost allocation. *Id*.

Bonneville agrees that any attempt to allocate costs to the IP rate must be consistent with the rate directives of section 7 of the Northwest Power Act and in particular the rate directives specific to the development of the IP rate. That said, the purpose of this proceeding is not to address issues that might or might not be raised in a future section 7(i) process or to determine what issues could properly be raised in that context. Bonneville can only comprehensively address the issues that are now before it in this proceeding.

Regardless of the procedural context, Bonneville must in the first instance have a legal basis upon which to seek recovery of the funds. Bonneville does not have the latitude to allocate costs to a customer class through a rate adder or surcharge as an administrative expedience without fully considering all of the applicable legal standards. In other words, a rate adder or surcharge is only a vehicle by which to recover funds, not a right to recover standing alone. As explained above, Bonneville does not believe that principles of law and equity, as discussed above, support such a right.

Moreover, even if some legal basis existed for taking such an action, there are practical impediments to implementation of any attempt to recover funds through ratemaking. There is nothing to prevent Alcoa from terminating its current contract with Bonneville if, for example, some sort of surcharge were considered or imposed. Today, Alcoa buys 75 aMW of power from Bonneville under its contract, which expires in 2022, and purchases the majority of its power from the open market. Alcoa can terminate its contract with Bonneville at any time pursuant to the terms specified in the contract. Initiating a section 7(i) proceeding to target Alcoa's existing rate with a surcharge or adder could trigger a contract termination by Alcoa, which would be effective one year from the date of notice. Indeed, Alcoa initially provided notice of termination of its present contract, and Bonneville and Alcoa thereafter negotiated an amendment reducing the amount of power purchased to the 75 aMW. Thus, Bonneville believes the risk of contract termination is neither conjectural nor unlikely. Bonneville would essentially place at risk a load that is economically advantageous to Bonneville and create a potential result that would not only render such ratemaking efforts irrelevant, but also result in lost revenue.[3]

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[3] Alcoa recently provided a notice of curtailment but has not terminated. Alcoa will continue to purchase some amount of power once the period of curtailment begins. At the present time, there is no indication that the curtailment will ultimately result in termination or have any significant unanticipated effects.

Lastly, Alcoa argues that administrative offset is not available because, in effect, there is nothing to offset:

> As a practical matter, BPA does not pay Alcoa money to which it might apply an offset . . .—quite the contrary, Alcoa pays BPA money for power BPA delivers to Alcoa. This effectively renders BPA's offset right a nullity.

Alcoa Initial Comments at 17. Bonneville agrees that presently there are no outgoing payments to Alcoa that would be available for set off against payments made under the Amendment. *Id.* Accordingly, for all these reasons, Bonneville believes that administrative theories of recovery, including administrative offset or a rate surcharge, would not provide a viable basis for a recovery of the funds expended under the Alcoa Amendment.

6. Evaluation of Cases Cited by PPC in Response to the DROD

In its response to the DROD, PPC identified case law it believes Bonneville failed to consider. PPC cites numerous cases for the proposition that the government has the authority to recover funds erroneously or illegally paid. PPC DROD Comments at 2-3. In particular, PPC cites *Old Republic Ins. Co. v. Fed. Crop Ins. Corp., 947 F.2d 269, 275 (7th Cir. 1991), United States v. Wurts,* 303 U.S. 414, 415-16 (1938), and *City of New Orleans*, 371 F.2d 21, 28 (5th Cir. 1967). Those and other cited cases are evaluated below.

a) ***United States v. Wurts.*** PPC cites *Wurts* and its progeny for the proposition that "the Government by appropriate action can recover funds which its agents have wrongfully, erroneously or illegally paid . . . " PPC Comments, at 3. However, Bonneville believes that the existence of a common law right to bring suit is not a waiver of pleading requirements under the Federal Rules of Civil Procedure, which require that the plaintiff, even if it is the United States, state a claim for relief that has some basis under the common law, in most instances a cause of action sounding in contract or tort or a recognized equitable claim.

   For that reason, Bonneville believes the words "by appropriate action" qualify the sentence in this fundamental respect. The sentence does not say the Government has the categorical right to recover erroneously or illegally paid funds. Rather, the government can only recover funds unlawfully or erroneously paid by bringing an appropriate action, that is, an action that is sufficiently meritorious that the government has a legal or equitable right to recover the amount claimed.

   Bonneville has never asserted that the government has no right to bring an action against Alcoa. To be clear, Bonneville agrees that it has the authority to recover funds erroneously or illegally paid and is statutorily authorized to do so. Indeed, it is only because BPA agrees it has such authority that Bonneville has taken the next steps to identify and analyze its likelihood of success under various legal

theories. The problem, however, is that after thoroughly evaluating each of these legal theories, Bonneville has concluded that, while it has the authority to bring these claims, ultimately Bonneville would not be likely to succeed on the merits. Bonneville believes that *Wurts* and the other cases cited by PPC do not significantly improve Bonneville's likelihood of success.

Moreover, *Wurts'* stands, in part, for the proposition that the government has a common law right of action where there is no statutory authorization for filing a civil action. *Wurts* has limited value in this instance because Bonneville's enabling statute provides the specific statutory authorization lacking in *Wurts*. Section 12(b) of the Bonneville Project Act states, in pertinent part: "The Administrator may, in the name of the United States, under the supervision of the Attorney General, bring such suits at law or in equity as in his judgment may be necessary to carry out the purposes of this chapter."

As a result, Bonneville believes that its role in responding to the remand is primarily defined by the Administrator's authority under section 12(b) to file actions based in law or equity "as in his judgment may be necessary to carry out the purposes of the act." In order to properly exercise his or her judgment under section 12(b), the Administrator must necessarily be advised of whether there is a cause of action that has a reasonable chance of success on the merits, not just whether a statutory and common law right to initiate such an action exists.

Further, section 12(b) requires the Administrator to coordinate with the Department of Justice, under whose supervision and direction any proposed litigation must be undertaken. Indeed, as the attorneys for the United States, the ultimate decision whether to initiate and pursue civil litigation would rest with the Department of Justice, not Bonneville

b) ***Old Republic Ins. Co. v. Fed. Crop Ins. Corp.*** PPC states that Bonneville has not given adequate consideration to *Old Republic*, which was cited in *ICNU*, and contends that, under that case, "even if the statute did not provide express authority for the government to recover its overpayments, 'the recovery is authorized by the government's common law right to recover improperly paid funds.'" PPC DROD Comments at 3. Again, this quotation goes to the question of whether Bonneville has the authority to bring a claim for the recovery of funds, but not to the question of whether Bonneville would prevail on such a claim.

In *Old Republic*, the Court found that the Federal Crop Insurance Corporation ("FCIC") was entitled to recover overpayments made to insurers under the Federal Crop Insurance Program. In that case, Old Republic Insurance Company entered into reinsurance agreements with the FCIC. FCIC initiated an investigation into payments made to Old Republic and determined that it had overpaid some claims. FCIC asserted a right to recover the overpayments, and Old Republic argued that FCIC lacked the statutory authority to recover the overpayments. The Court disagreed, finding in the first instance (as in *Wurts*) that

the government has the general right to recover unlawful or excessive payments and there was no statutory bar that would preclude FCIC from doing so.

Next, the Court evaluated the facts in the context of the language of the contracts between the FCIC and Old Republic. The Court found that various provisions of the contracts "contemplated the reconsideration of claims and the recovery of wrongfully paid money from the [FCIC]." *Id*. at par. 11. The Court then found that the overpayments were the direct result of actions taken by Old Republic: "the FCIC is seeking immediate repayment only of those overpayments caused by Old Republic's negligent or wrongful conduct." *Id*, par. 18, 21. The court explained that to permit Old Republic to retain these funds would reward Old Republic for its own malfeasance. *Id*. at 18.

In the present case, this element of wrongful conduct is missing. Although PPC cites *Old Republic* for the proposition that the government has a common law right to recover erroneously paid funds, *Old Republic* is essentially based on a cause of action involving contract law. The court found that the FCIC had a contractual right to obtain overpayments, and the overpayments were caused by Old Republic's own misconduct. In contrast, the Alcoa Amendment does not contain any language authorizing the recovery of wrongfully paid funds by Bonneville, and there is no conduct on the part of Alcoa that could be equated with or analogized to Old Republic's negligent or wrongful conduct.

Although *Old Republic* supports the general proposition that the government has the authority to recover erroneously paid funds, as pointed out above, that proposition is not in dispute. Given the factual and legal distinctions between *Old Republic* and the Alcoa Amendment, Bonneville believes that *Old Republic* does not assist Bonneville or increase its likelihood of success on the merits in a claim against Alcoa.

c) ***Federal Crop Ins. Corp. v. Merrill***. PPC's comments on the DROD include a block quote from *Federal Crop Ins. Corp. v. Merrill*, 332 U.S. 380, 383-84 (1947), for the proposition that a recipient of government money is not entitled to retain funds unlawfully disbursed regardless of whether the recipient engaged in improper conduct. PPC DROD Comments, at 3-4. PPC contends that, in light of *Merrill*, Bonneville's claim of unjust enrichment against Alcoa should succeed because, even if Alcoa was not at fault or responsible for the illegal disbursement, Bonneville is nevertheless entitled to a recovery of the funds. *Id*. A close review of *Merrill*, however, presents a very different factual scenario.

In *Merrill*, the FCIC issued an insurance policy to a farmer for crop losses. The farmer was expressly advised by an agent for the government that his crop was insurable and, as a result, the policy was applied for and issued. The farmer lost his entire crop due to drought and sought reimbursement from the FCIC. The FCIC refused to pay because the insurance application was explicitly subject to all relevant regulations as published in the Federal Register, one of which precluded

recovery for the type of loss sustained by the farmer. The farmer filed suit against the FCIC and was successful in the lower courts. The Supreme Court reversed and held that, even though the farmer was wrongly advised by a government agent that his crop was insured, the regulation prohibited FCIC from paying funds in this circumstance.

In some ways, this case could be said to represent the concept that a party doing business with the Government must "turn square corners" and know what the law is. Equally significant, however, is that, when dealing with the government, there is no doctrine, as can be found in the private sector, that statements made by an agent having apparent authority are sufficient to bind a party. In dealings with the Federal government, by contrast, a party is entitled to rely only on those agents who possess actual authority. *Merrill* discusses this rule as follows:

> Whatever the form in which the Government functions, anyone entering into an arrangement with the Government takes the risk of having accurately ascertained that he who purports to act for the Government stays within the bounds of his authority. The scope of this authority may be explicitly defined by Congress or be limited by delegated legislation, properly exercised through the rule-making power.

In *Merrill*, there was an existing regulation promulgated by the FCIC, stating explicitly that the kind of crop in question could not be covered by the policy in the event that it was destroyed by drought. The agent who stated otherwise had no authority to waive that regulation. Therefore, the court would not permit recovery in spite of both the agent's incorrect representation that the crop was insurable and the hardship suffered by an insured. Whether a party is entitled to rely on the representations of the Bonneville Administrator, in matters pertaining to contracting for power sales, presents a very different question, particularly where there was no explicit statute or regulation that prohibited continuation of a monetized arrangement.

Further, although PPC cites *Merill* to support an unjust enrichment argument, *Merrill* is not an unjust enrichment case. On one level, *Merrill* is an insurance contract case where an insured sought to obtain payment under the policy that was subject to relevant regulations that were essentially incorporated as contract terms, and one of those existing regulations prohibited the disbursement for the crop in question. The insured essentially argued that the government's agent had waived a specific regulatory requirement and the government should not be permitted to deny payment under the circumstances. The court disagreed and found that the agent had no authority to waive an existing regulation and the insured was responsible for knowing the law.

As to the issue of unjust enrichment, because no funds were ever disbursed in *Merrill*, no benefit was ever conferred and so the insured was never enriched, unjustly or otherwise. Since the insured never received a benefit, there was no

possibility of a benefit being retained and no basis upon which to conclude that its retention under the circumstances would be unjust. Thus, the case does not stand for the proposition that Bonneville could obtain a recovery under an unjust enrichment theory or that it could do so without satisfying all of the standard elements of such a claim, described above.

As noted elsewhere, Bonneville did conclude that Alcoa had been enriched by the payment, but also concludes that it could not demonstrate that Alcoa engaged in any improper conduct like fraud, misrepresentation, duress, or even inducement that would be necessary to prevail on such a claim. Nothing in *Merrill* alters those conclusions.

d) ***United States v. United Technologies*, 2012 U.S. Dist. WL 2263280 (D. Ohio, 2012).** PPC also cites *United States v. United Technologies*, 2012 U.S. Dist. WL 2263280 (D. Ohio, 2012) for the proposition that, in finding for the government on its common law claim of payment by mistake, the only causation required is causation in fact. PPC DROD Comments, at 4. However, *United Technologies* is not simply a case involving the government's ability to recover funds under a common law theory of payment by mistake. It is a case where the court determined, among many other things, that the government was defrauded by the contractor's material misrepresentations, resulting in the government being awarded over $657 million in damages against the contractor, based in part on obtaining treble damages under the False Claims Act. *Id*. at 8; *see also United States v. United Technologies,* 949 F.Supp.2d 952-53 (S.D. Ohio 2013). United Technologies also retained a substantial amount due to the fact that the government materially benefitted from jet engines provided under the contract that were not subject to fraud or misrepresentation. The case is also materially distinguishable on the facts and law. Moreover, *United Technologies* is an extremely complex case, procedurally and factually, with a seventeen year history of litigation between multiple parties in multiple venues. *See United States v. United Technologies,* slip op. at __ 6th Cir., April 2015). It is not surprising that the case is also subject to a large amount of negative history, which further undermines it as authority for the proposition cited by PPC.

e) ***United States v. Independent School District No. 1 of Okmulgee County, Oklahoma.*** PPC cites *United States v. Independent School District No. 1 of Okmulgee County, Oklahoma*, 209 F.2d 578, 580 (10th Cir. 1954) for the proposition that the government can file claims for restitution and unjust enrichment for disbursements due to mistake of fact. In that case, the government disbursed funds to a state school district pursuant to a federal program to provide financial assistance for school lunches. The school district submitted invoices to the federal government for reimbursement, which the government paid. Following an audit, it was determined that the school failed to maintain adequate records to substantiate its invoices as required by the agreements. As a result, there were overpayments made by the government that could be collected. The court held that the issue of whether the government could successfully recover

was a matter of federal law, not state law, and ultimately the court entered judgment for the United States.

The PPC is correct that this case supports a claim by the federal government for restitution of an overpayment of financial assistance. It is not clear, in this instance, however, what mistake of fact could be relied upon in that the payments were not mistaken as a factual matter. They were made in the amount agreed to by the parties to a contract, not in response to invoices that were not reliable. To the extent that the mistake doctrine is applicable, any mistake was a mistake of law based on the Administrator's understanding of the implications of the *PNGC I* opinion at the time the contract was made.

It is also significant that in *Independent School*, if not for the inadequate records and erroneous invoices provided by the school district, there would have been no overpayment. Because the school district induced the government to relinquish the benefits by filing invoices that could not be substantiated, and was unable to provide the material facts that were a predicate for the government's relinquishment of the benefits, the case falls within the parameters of a claim for unjust enrichment, as articulated elsewhere in this ROD. In short, the school district was enriched due to its own malfeasance – similar to the situation in *Old Republic*, discussed above. If anything, the case supports Bonneville's view that recovery is dependent upon having a meritorious cause of action to support its claim and, in the case of unjust enrichment, some wrongful act on the part of the person receiving the benefit.

In this case, as stated elsewhere, there is no credible argument that Alcoa engaged in improper conduct that led to payments made pursuant to the Alcoa Amendment. If anything, given the circumstances as described elsewhere, Bonneville believes a court would likely find Bonneville primarily responsible for misinterpreting its own statutory authorities and making a contract offer based on its erroneous view of the standards which the court would later apply. Because Alcoa did not use any means to induce Bonneville to enter into the Amendment or make the payments, there is not a sufficient factual basis to support all of the elements of an unjust enrichment claim.

(f) ***Stone v. United States***. *Stone v. United States*, 286 F.2d 56 (8th Cir. 1961), is similar in important respects to *Merrill*. In *Stone*, an operator of a wool producing business attempted to qualify for payments by the federal government for the sale of wool under National Wool Act of 1954. To obtain payments, the applicant needed to provide invoices showing, among other things, sales of wool and acceptance by the buyer. The wool business operator inquired of a government agent whether he could sell the wool from sheep on his own farms to his own wool manufacturing house. He was advised that such sales would qualify provided that it was supported by bona fide evidence of the transaction.

The defendant provided the requisite paperwork and the funds were disbursed by the government. Subsequently, the government determined that the funds were wrongfully paid because the defendant was acting as both buyer and seller, which did not comport with the statute or its implementing regulations. The government sued for recovery of the funds under multiple theories, including mistake of law and fact. The defendant argued against recovery, alleging the estoppel against the government as well as detrimental reliance, and as a matter of equity, that he should be entitled to retain the payments.

The lower court ruled in favor of the government on summary judgment on the theory of mistake of law and fact, and the issue on appeal was whether the case was appropriate for summary judgment due to issues of material fact that were arguably in dispute. *Stone* is instructive because it involves a disbursement of funds by the government, and the court found the government was entitled to recovery because, under the regulatory program, the defendant was prohibited from being reimbursed if he was both the buyer and seller. The program was designed to provide assistance to wool producers, but not if they were on both ends of the deal. Notably, even though the wool producer was misinformed by an agent of the federal government, it was the actions of the wool producer acting as both buyer and seller that prohibited him from being eligible for the funds in the first place.

In the case of the Alcoa Amendment, there is no similar or analogous conduct on the part of Alcoa. It was Bonneville, not Alcoa, who offered a contract amendment to provide for the payment of funds in a manner that Bonneville determined complied with the law. Alcoa did not take any action that was prohibited by statute or regulation. Ultimately, it was determined that Bonneville did. To be sure, Alcoa accepted Bonneville's offer because it was in its business interests to do so. But Alcoa did not engage in any improper activity that was the impetus for Bonneville disbursing the payments to Alcoa.

Another limitation of *Stone* is that, because it is a summary judgment case, the facts are not well developed. Although the case notes that the defendant raised an argument of detrimental reliance, the nature of its reliance and the strength of that argument is not addressed in any meaningful fashion in the opinion. In contrast, Bonneville believes that Alcoa's claim of detrimental reliance is such a fundamental part of its case that the likelihood of Bonneville succeeding in a summary judgment motion is extremely low, and conversely, the likelihood of a court developing a full factual record on the detrimental reliance argument (and all other factual arguments) is extremely high.

(g) City of New Orleans v. United States. In *City of New Orleans v. United States*, 371 F.2d 21 (5th 1967), Chrysler entered into a contract with the United States to purchase and install equipment in a military ordnance plant. Chrysler purchased the equipment and the city of New Orleans assessed a use tax on Chrysler for the purchased items. Chrysler paid the tax in escrow under protest. Following

unsuccessful state court litigation, the United States and Chrysler filed suit in federal court for recovery of the funds, arguing that Chrysler acted as an agent of the Government, and by taxing Chrysler, the city was in fact taxing the Government, which it lacked authority to do. The lower court granted summary judgment for the United States, and the court, on appeal, affirmed, noting that "there is ample power in the United States District Court to protect the sovereign against such unjust enrichment of familiar principles of money had and received . . . This harmonizes with the usual principle that Federal law fashions remedies for recovery of funds or property of the United States – including those from invalid tax exactions." *Id*. at 28.

City of New Orleans stands for two propositions: first, federal courts are the proper forum for the federal government to obtain relief from improper city or state taxation, and second, in so doing, federal courts will protect the government from unjust enrichment. In *City of New Orleans*, there is no question that the city was unjustly enriched: by taxing an agent of the federal government, the city taxed the federal government itself, which it lacked the power to do. Summary judgment was appropriate because, as a matter of law, the city could not tax the federal government and there were no material facts in dispute.

In the case of the Alcoa Amendment, the central issues in dispute are whether Alcoa was enriched, and if so, whether the enrichment was unjust. Bonneville has concluded that Alcoa was enriched, but that Bonneville would not prevail on demonstrating that Alcoa was enriched unjustly. For these reasons, the type of legal and factual issues at the heart of the dispute regarding the Alcoa Amendment were not even debated in *City of New Orleans*. Because, as a matter of law, the tax was improperly assessed against the federal government, the city was necessarily unjustly enriched. There was nothing more for the court to consider. For these reasons, Bonneville believes *City of New Orleans* is materially distinguishable from the Alcoa Amendment.

In conclusion, while Bonneville understands the preference customers' positions, and appreciates the effort to apprise Bonneville of a wider range of cases than had been previously evaluated, the cited authorities do not significantly alter Bonneville's view that a successful outcome is unlikely given the facts and circumstances of this case.

7. Evaluation of PPC's Reliance of Treasury/BFS Guidelines.

PPC also attached to its comments a treatise issued by the Bureau of the Fiscal Service (BFS) under the Department of Treasury entitled Treatise of Federal Nontax Debt Collection Law (Treatise). As discussed above, Bonneville believes that the cases cited in the PPC's comments do not support the proposition that Bonneville has a likelihood of success on the merits given the facts of this case. With respect to the attached Treatise on Federal debt collection, it is not entirely clear how PPC believes this document advances its position. PPC urges Bonneville to review the treatise and "explain why, given the

authorities cited in these comments and in the [Treatise], BPA appears to believe it has no viable common law claim for recovery of the unlawful payments from Alcoa." Comments, at 5.

Bonneville has reviewed the Treatise to determine the extent to which it supports PPC's position that Bonneville has a viable common law claim for recovery. Notably, the Treatise is essentially a compilation of debt collection law which discusses various mechanisms for administrative recovery of debts. As noted in the Introduction to the Treatise, "the purpose of this Treatise is to provide federal agency counsel and program staff with an in-depth explanation and interpretation of the laws that govern administrative collection of federal nontax debts."

As PPC correctly notes in its comments, an "Eligible Debt" under the Debt Collection Act is as "any amount of funds or property that has been determined by an appropriate official of the Federal Government to be owed to the United States . . . " Section V(b)(1). For a debt to be eligible for administrative offset, it "must be determined to be due by an agency official." Section V(b)(2).

A review of these definitions and introductory comments demonstrate that the Debt Collection Act primarily serves a different purpose than that suggested by PPC, *i.e.*, to employ as a basis for pursuing a claim under the common law. Instead, it is directed toward the administrative collection of bona fide debts, a designation that is only applicable where there is a determination by an authorized agency official that a debt is due and owing. In this case, Bonneville has never determined that Alcoa owes a "debt" to Bonneville, as that term is used in the Debt Collection Act. Similarly, although the Ninth Circuit found that Bonneville exceeded its authority when it made payments to Alcoa, it never determined that Alcoa is a debtor under the Debt Collection Act. Indeed, the issue was never addressed, discussed or briefed. In fact, it would be surprising if the Court were to make such a designation in light of the DCA specifying that the decision rests with agency officials rather than the courts.

Equally important, the Treatise explains that an agency may not attempt to collect a debt under the Debt Collection Act without providing the alleged debtor due process. Section V(B)(3) of the Act states, "the United States may not deprive a person of property without first providing due process . . . Offset is a governmental action and is a deprivation of property." As a consequence, a federal agency cannot simply decide that a debt is due by administrative fiat. In a case such as this, where an alleged debt has been vigorously disputed from the time the initial DSI Lookback was first undertaken, it would not be appropriate to launch an administrative collection action without first providing some kind of due process, which would most likely commence by initiating the dispute resolution process specified in the contract between Alcoa and Bonneville. It is also important to recall that, in this case, there are no outgoing revenues in connection with the Alcoa contract against which the most obvious self-help remedy of offset could be taken in the first place. Thus, Bonneville believes that asserting that Alcoa owes BPA a debt would not satisfy the standards set forth in the Debt Collection Act or place Bonneville in any better position than the one it now occupies.

Even if, for the sake of argument, Bonneville made a determination that Alcoa was a debtor under the Debt Collection Act, Alcoa would necessarily challenge that determination. As Alcoa has indicated, its challenge would, at the outset, trigger the dispute resolution requirements of the contract. The likely course of events would be that the parties would be unable to resolve the dispute, as was the case earlier this year when Bonneville provided such an opportunity for settlement prior to commencing this process. At that point, the contract specifies that disputes are to be resolved pursuant to the requirements of the Contract Disputes Act. Assuming that is the appropriate litigation path, it would ultimately lead to adjudication by the Court of Federal Claims, where all legal and equitable arguments discussed in this record of decision would be litigated *de novo*. Thus, the issue of whether Alcoa could be definitively considered a "debtor" under the Debt Collection Act or otherwise would be entirely contingent on the outcome of that litigation.

For these reasons, a determination by Bonneville that Alcoa is a "debtor" would not in itself result in Bonneville obtaining the expended funds or improve the probability of Bonneville successfully recovering them. Rather, it would simply raise another disputed issue to be resolved ultimately by a judicial proceeding where Bonneville would be required to prove that it is entitled to such a recovery based on a meritorious cause of action. As such, Bonneville does not believe that, if Bonneville were to proceed along the lines advocated by PPC, the Debt Collection Act or the submitted Treatise diminishes the prospect of adjudication of this matter by a court with competent jurisdiction or enhances Bonneville's prospects of recovering the expended funds to any degree.

C. Analysis of Alcoa's Claim for Net Underpayment

Alcoa introduces its analysis of its claim for net underpayment by stating that "if BPA pursues recovery of the MB payments, Alcoa has viable claims against BPA, cognizable in the United States Court of Federal Claims, to recover (a) the costs it incurred under the monetized contracts and (b) the value of the benefits it conferred upon BPA pursuant to these agreements." Alcoa Initial Comments at 2. It should be noted that, on the level of balancing the equities in litigation initiated by Bonneville pursuing restitution, the arguments posited by Alcoa might be more viable than if they were asserted affirmatively.

Regardless, viewing the claims as presented in Alcoa's comments, Bonneville concludes that they have little merit. Bonneville is not persuaded by Alcoa's attempt to depart from the clear language and intent of the Block Sale Contract by arguing that Bonneville essentially bargained away its protection under the damage waiver provision. Nor does BPA believe that Alcoa has a credible argument that the Block Sale Contract was essentially supplanted by an "implied in fact" contract that gives rise to the remedy of *quantum meruit* and/or *quantum valebant*.

1. Legal Status of the Block Sale Contract Damage Waiver Provision

In its comments, Alcoa cites the mutual damage waiver as follows:

> In the event the Ninth Circuit Court of Appeals or other court of competent jurisdiction issues a final order that declares or renders this Agreement void or otherwise unenforceable, no Party shall be entitled to any damages or restitution of any nature, in law or equity, from any other Party, and each Party hereby expressly waives any right to seek such damages.

Alcoa Initial Comments at 27. The language could hardly be more clear, and both Alcoa and Bonneville argued before the Ninth Circuit that the damage waiver was mutual, applying equally to both parties. Nonetheless, Alcoa now asserts that the waiver is unilateral. Alcoa contends that the damage waiver precludes Bonneville from raising any and all claims against Alcoa arising out of the Block Sales Contract, but that it does not apply similarly to Alcoa. Alcoa's argument directly contradicts the express contract language, the intent of the parties, positions taken by Alcoa in litigation before the Ninth Circuit, and the *ICNU* opinion upholding the damage waiver as applying mutually to both Alcoa and Bonneville.

First, Alcoa claims that the "[t]he Block Contract's damages waiver applies to bar only those claims occurring during the period in which that waiver was in effect." *Id.* BPA takes this to mean that Alcoa claims the damage waiver is not applicable to damages that arose out of that contract if the damages were allegedly sustained after the Block Sale Contract terminated. That is not what the provision says. The damages waiver has no such limitation and no sunset clause. The protection afforded by the damage waiver survives expiration or termination of the Block Sale Contract, and the damage waiver, by its terms, bars Alcoa from pursuing claims for damages arising from the Block Sale Contract irrespective of when those alleged damages may have occurred.

Second, Alcoa argues that the damage waiver provision was revoked by the terms of a subsequently executed contract –the Equivalent Benefits Contract. This argument is based on the premise that the Ninth Circuit allegedly "overturned" BPA's Lookback ROD that was under review in *ICNU*. *Id.* at 28. However, the ROD was not overturned. On the contrary, the Court expressly upheld the damage waiver provision and the portion of the ROD that pertained to the Block Sales Contract. It only remanded for further consideration the portion of the ROD that pertains to the Alcoa Amendment, which did not include a damage waiver.

In conclusion, despite Alcoa's arguments to the contrary, the damage waiver provision is clearly mutual and bars any claim by Alcoa against Bonneville that may arise from the Block Sale Contract, regardless of whether the claim arose before or after termination of the agreement.

2. Claims Based On the Alcoa Amendment.

Alcoa claims that it incurred damages of approximately $35 million during the period of the Alcoa Amendment. Alcoa disputes this calculation in later comments and its objection is noted but points out that Bonneville's assessment is predicated on the comment cited below. It does not seem particularly useful, at this time, to dedicate any discussion to resolving the alleged discrepancy. For now, the important issue is that the claim is based on the theory that, if Bonneville had sold physical power to Alcoa during the amendment period rather than provide monetary payments, it would not have suffered its alleged losses. As explained by Alcoa:

> During the period of the Alcoa Amendment (December 1, 2008 to September 30, 2009), Alcoa paid $131,447,016 for power, and received $25,686, 868 in MB payments . . . Alcoa's net power costs were therefore $105,760,148. Had Alcoa purchased physical power at the IP rate, however, it would have paid only $70,912,726. Thus Alcoa over paid by $34,847,422 during the period of the Alcoa Amendment, even taking into account the MB payments it received.

Alcoa Initial Comments at 8.

Alcoa's argument is defective for three reasons. First, despite Alcoa's arguments to the contrary, it voluntarily elected to execute the Alcoa Amendment and receive the monetized payments. By receiving these payments, Alcoa's purchased power costs were reduced, dollar for dollar, by the monetary benefit payments. As explained earlier, this is not an injury, it is a benefit. Although Alcoa may have preferred a better deal – whether greater payments or physical power – it nevertheless received substantial financial benefits from the transaction. Alcoa made a reasonable business decision to execute the agreement because it was in its business interests to do so.

Indeed, following issuance of *PNGC I*, it was clear by the Court that service to Alcoa was discretionary, as Bonneville had determined years prior to that opinion. Bonneville had no obligation to sell power to Alcoa at all, regardless of whether it was physical power or a monetized transaction. Alcoa appears to rest its argument on the premise that, in *PNGC II*, the Court found that if Bonneville offered to sell power to Alcoa, it must first do so with an offer of physical power at the IP rate. However, it is equally true that, as noted, Bonneville had no obligation to offer to sell power or to provide monetary benefits at all. Therefore, Alcoa is essentially arguing that it has been damaged by not receiving the benefits of a contract that was never offered and consequently never existed. It is not credible for Alcoa to now contend that Bonneville is somehow responsible for those purely hypothetical losses when Alcoa received substantial benefits - $25.6 million - at a time when it was entitled only to the specific benefits agreed to by the parties.

Second, Alcoa's argument is further weakened by the fact that, at the time the amendment was executed, Alcoa had already purchased physical power under the Block Sales Contract to serve its load for the period covered by the Alcoa Amendment. As a result, a sale of physical power from Bonneville was unnecessary—and may well have

been undesirable from Alcoa's perspective at that time (a point now contested by Alcoa)—since a power supply had already been secured.

Third, Alcoa received the full benefit of its bargain. It received full payment under the Amendment up until the Court issued its opinion in *PNGC II*. Alcoa is essentially arguing that it is entitled to not only the monetary benefits it received, but also is entitled to any perceived losses it may have incurred as a result of its own business decision. However, Bonneville never agreed to be responsible for Alcoa's risk associated with purchasing power on the market. On the contrary, the whole point of the monetized transaction was to provide cost certainty to Bonneville and shift the risk of market purchases to Alcoa. Alcoa's theory turns the agreement on its head by ignoring the basis for the bargain and shifting all the costs and risks associated with market purchases back to Bonneville.

In short, Bonneville is not responsible for indemnifying Alcoa for the consequences of its own business decisions. Contrary to Alcoa's assertions, Bonneville did not force or coerce Alcoa into executing the Alcoa Amendment, or for that matter, the Block Sales Contract. Alcoa received full payment under the contract up until the date it terminated due to the *PNGC II* opinion, which is all it was entitled to receive. For these reasons, Bonneville believes Alcoa's affirmative claim of damages is not viable and would not prevail. However, as noted earlier and discussed more fully below, Bonneville believes Alcoa's arguments would carry more weight as defenses or counterclaims to an action initiated by Bonneville.

3. **<u>Implied in Fact Contract and Quantum Meruit/Quantum Valebant</u>**

Alcoa's comments explain the legal theory that it would follow were its claims ultimately heard by the Court of Federal Claims, which it describes as a "Quantum Meruit/Quantum Valebant claim." Alcoa Initial Comments at 30. While those doctrines actually go to the remedy Alcoa would be seeking, Alcoa posits a theory based on an "implied in fact" contract:

> Alcoa will have little difficulty establishing the existence of an implied-in-fact contract between Alcoa and BPA. The Federal Circuit has "identified four requirements of an implied-in-fact contract: (1) mutuality of intent to contract; (2) consideration; (3) lack of ambiguity in offer and acceptance; and (4) actual authority in the government representative to bind the government." To establish the first three elements Alcoa need only show that, once the unlawful MB provisions of the Block Contract and Alcoa Amendment are struck out, these express contracts "simply incorporate[] an implied-in-fact promise by the government to pay at least fair market value" for the benefits delivered by Alcoa under the contract.

Id.

This argument is based on a false premise. There were express contracts - the Block Sale Contract and the Alcoa Amendment - defining the rights and obligations of the parties. These contracts were fully performed according to their terms, except to the extent such performance would have been inconsistent with court orders. The existence of these express contracts and the fact that the expected value was provided thereunder negate the proposition that an implied in fact contract governing the same subject matter should be interposed to provide Alcoa with a windfall far beyond its expectancy interest, especially when no value accrued to Bonneville as a result of the contract, beyond what was originally contemplated by the parties at the time of contracting.

Suffice it to say that, both parties entered into the Block Sale Contract and Alcoa Amendment based on their own considerations, business or otherwise, and both received the agreed to value for their performance. That is essentially the beginning and end of any implied in fact contract theory.

Quantum valebant and *quantum meruit* are available to provide equitable compensation to contractors who, despite a defective contract, have provided goods and services that are accepted by and beneficial to the government. They are not available, as proposed by Alcoa, to enlarge by hundreds of millions of dollars the consideration that was essentially bought and paid for under the terms of an express agreement.

Bonneville's final determination is that Alcoa's claim for relief against Bonneville, as an affirmative claim, has no merit.

4. Evaluation of Alcoa's Comments in Response to DROD

Alcoa raises numerous complaints about Bonneville's approach in the DROD and essentially argues that in all instances Bonneville's analysis is defective, either because it does not go far enough or because, in Alcoa's opinion, it is flatly wrong. Bonneville does not agree with Alcoa's assessment. Previously in the DROD and now in this final ROD, Bonneville has laid out the basis for its legal view of this case. Even in light of numerous cases cited by PPC, Bonneville has reached the conclusion that application of basic legal and equitable principles casts substantial doubt on its ability to recover the $25.6 million spent pursuant to the Alcoa Amendment. That conclusion is based primarily on the weaknesses that Bonneville has identified in its affirmative case rather than a positive view of the merits of Alcoa's case as an affirmative claim.

Thus, even in light of Alcoa's additional comments on the DROD, Bonneville continues to believe that Alcoa would have an uphill battle to bring a successful affirmative claim against Bonneville. On certain issues, as shown elsewhere in the ROD, Alcoa and Bonneville will have to continue to disagree. However, some additional analysis is also provided assessing the strength of Alcoa's position as a defense, counterclaim, or offset to damages. On that score, Bonneville generally gives Alcoa's arguments more weight if they were presented in the context of defending against Bonneville's claim as a matter of balancing the equities of the facts and circumstances present here.

a) Alcoa's Comments on Bonneville's Analysis of Recovery Theories

Alcoa begins by challenging Bonneville's actions in stopping payments under the Amendment when the Ninth Circuit issued *PNGC II*.

> . . . .BPA did not, strictly speaking, fully perform its obligations "in accordance with the express contract terms." The terms of the Alcoa Amendment provided that Alcoa would receive approximately $32 million in monetary benefit payments over the term of that agreement. Because of the decision in *PNGC II*, however, BPA terminated these payments after July 2009, prior to the expiration of the Alcoa Amendment period. Though of no consequence to a BPA breach-of-contract claim, the fact that Alcoa fully performed under the Alcoa Amendment but did not receive the entire benefit for which it had contracted is relevant in analyzing the parties' other claims, and should be duly noted in the Final ROD

Alcoa DROD Comments at 7. Bonneville's position is that all of its legal obligations were satisfied. When the Court rendered its opinion in *PNGC II*, Bonneville was essentially relieved of any further performance obligations. Any attempt to continue payments would have been a direct violation of the Court's order. It is highly unlikely that Alcoa could successfully argue that it had any legal right to further payment in light of that order.

Alcoa goes on to the claim that its contractual dealings with Bonneville constitute contracts of "adhesion":

> Finally, the Draft ROD here improperly downplays the position into which BPA had placed Alcoa. . . . The Alcoa Amendment was not the sort of arms-length agreement BPA here and elsewhere in the Draft ROD makes it out to be; it was BPA's temporary, take-it-or-leave-it solution to the problems BPA itself created by insisting on the Block Contract instead of a lawful sale of physical power at the IP rate. Similarly, that the Alcoa Amendment shifted the risk of market fluctuations to Alcoa is simply one reason why that agreement was unlawful (and an example of a benefit BPA obtained at Alcoa's expense)—not evidence that Alcoa alone should bear its costs. To the extent that BPA addresses this issue under this heading in the Final ROD (and, being irrelevant to BPA's breach-of-contract claims, it need not), BPA should make these findings in the Final ROD, or at least acknowledge Alcoa's position and consider the risk that the Court of Federal Claims may ultimately be persuaded by Alcoa's argument.

Id. at 8. Bonneville does not object to acknowledging Alcoa's position but it does not believe that the Court of Federal Claims would likely be persuaded by such an argument. None of the contracts entered into are adhesion contracts. It is true that Bonneville may have had bargaining leverage with respect to the type of contract it was willing to offer. For various reasons, Bonneville was not willing to make the offer that Alcoa preferred,

i.e., actual power at the IP rate, but instead was only willing to monetize the transaction in order to hedge Bonneville's market risk.

More importantly, Alcoa was not a captive customer who had no other choice than to buy its power supply from Bonneville. Alcoa has its own power marketing division, which could readily have supplied Alcoa's power needs through a market purchase strategy without any reliance on Bonneville at all. Alcoa had a choice. It chose Bonneville's offer because it was in Alcoa's business interest to do so, not for any other reason. Neither the Amendment nor the Block Sales Contract was a contract of adhesion.

Alcoa then goes on to suggest that Bonneville's discussion of contract illegality is flawed because Alcoa does not believe, based on its reading of the case law, that the concept could be used in the context of an affirmative claim, as opposed to a defense. Id. at 9. This issue has more support in law and Bonneville essentially has taken the position that a court would probably apply the common law rule that parties to an illegal contract cannot avail themselves of the courts in order to enforce an illegal bargain. For example, the doctrine would come into play more aptly if Alcoa were to seek recovery of the remaining benefits that were not paid. Bonneville would in all likelihood successfully defend on the basis of illegality. Bonneville nonetheless believes, despite Alcoa's concern, that it was useful to discuss the issue as a potential Bonneville affirmative cause of action, due to case law cited by both Bonneville and PPC, that the government has a common law right to pursue monies that were illegally paid. Bonneville's conclusion remains, as in the DROD, that Bonneville's chances of prevailing on that basis are slim.

Alcoa is also not entirely satisfied with Bonneville's analysis of the mistake of law theory. *Id.* at 12. As stated previously, Bonneville does not believe that it would be successful raising a mistake of law claim against Alcoa. The theory is rarely successful and the facts and circumstances here provide little or no support for success in this case. Bonneville acknowledges that Alcoa believes that "[t]o the extent the doctrine of mistake of law is applicable to the instant matter at all, it would benefit Alcoa, not BPA" (citing *C & L Const. Co. v. United States).* Bonneville only notes in response that Alcoa's proposition is highly doubtful as well. Bonneville does concede Alcoa's point that "Federal Circuit precedent provides that in certain circumstances, government officials will be deemed to be authorized to commit mistakes of law, such that the government is estopped from denying the validity of the agreements that result therefrom." This lack of clarity is an issue that Bonneville took account of, perhaps not as directly as Alcoa would have preferred, in the legal risk assessment provided in the DROD. To the extent that was not clear, it should be now.

Alcoa then moves on to challenge certain aspects of Bonneville's analysis of a potential claim for recovery based on unjust enrichment. Id. at 12-15. Bonneville's conclusion is that, in all likelihood, Bonneville could demonstrate that Alcoa was enriched, but would be unable to show that Alcoa had engaged in any misconduct that would make it inequitable for Alcoa to retain the benefit received. Alcoa renews its argument that it was not enriched by the $25.6 million that it received pursuant to the terms of the Amendment. Bonneville understands Alcoa's position but, for the reasons stated above,

continues to believe a court would ultimately find that Alcoa was in fact enriched by payments made pursuant to the Amendment.

Alcoa also chides Bonneville for not acknowledging its potential defenses to an unjust enrichment claim and for relying on unpublished slip opinions that might not be permissible in a litigation setting. Regardless of the source material, Bonneville has acknowledged that Alcoa probably has the ability to successfully defend on the basis that it engaged in no misconduct that makes retention of the payments inequitable. However, the purpose of this public process is to reach a reasonable conclusion in this matter and, while some sources are more persuasive and perhaps entitled to more weight than others, at this point, the Administrator is taking a flexible view regarding the types of sources that may be cited or relied upon. The Administrator's aim is to provide a reasonably complete and fair evaluation of the legal principles at issue here.

Alcoa also states that Bonneville's numbers are inaccurate:

> Finally, BPA's numbers are incorrect. As explained in its previous comments, Alcoa paid an estimated $131,447,016 for power during the Alcoa Amendment period. After subtracting roughly $25.6 million in monetary benefit payments, Alcoa's net power costs during this period were an estimated $105,760,148. Purchasing that same amount of power at the lawful IP rate, however, would have cost Alcoa only an estimated $70,912,726. As a result, even after receiving monetary benefit payments, Alcoa paid an estimated $34,847,422 more for power during the Alcoa Amendment period than it should have at the lawful IP rate.

Id. at 15. Bonneville understands Alcoa's desire to preserve its arguments and acknowledges that Alcoa disputes Bonneville's calculation.

b) Alcoa's Comments in Response to Bonneville's Evaluation of Alcoa's Claim

Alcoa goes to a great deal of effort to buttress its purported claim against Bonneville. There is little point in belaboring issues that have been addressed before in light of Bonneville's decision that there is considerable doubt about Bonneville's ability to pursue a recovery effort successfully. Bonneville continues to believe that Alcoa's claim has little merit as an affirmative claim. However, as noted earlier and touched on in the DROD, Bonneville believes that Alcoa would be in a better positon to raise issues in defense of a claim lodged by Bonneville or as a counterclaim. In that event, Alcoa's arguments might well be framed differently than they have been in its comments, which have been more aligned with the approach set out in the Court's remand order.

In spite of Alcoa's renewed arguments, Bonneville's position has not changed. Bonneville continues to disagree with what it sees as Alcoa's effort to enlarge the scope of the damage waiver provision beyond anything contemplated by the parties. Those views are set forth above.

Similarly, Bonneville's position has not changed regarding Alcoa's posited implied-in-fact contract/*quantum valebant* theory. Again, Bonneville's views are stated above. Bonneville recognizes that it is sound policy for the courts to preserve the interests of those who are deprived of the benefit of their bargain with the United States government and its agencies through no fault of their own. However, Bonneville also believes that Alcoa's reliance on those doctrines in this instance is misplaced.

The principles used for protecting the interests of those who contract with the government are designed to provide a remedy for a contractor who did work expected under a contract, sometimes one that was later found to be defective for one reason or another. The contractor either incurred costs in performance of the government's contractual expectations and/or partially completed performance according to contract specifications. The government induced the reliance or received the expected performance and, in most instances, obtained tangible material value in terms of goods or services rendered, but the party contracting with the government was not paid, or not fully reimbursed, for one reason or another.

In this case, the costs that Alcoa incurred for purchasing power, and which now form the basis for its alleged damages, were simply necessary consideration for providing Bonneville with the value that it bargained for, *i.e.*, a hedge against volatile market prices, maintenance of the *status quo*, and the opportunity to keep open the opportunity for future transactions. Bonneville did not use or benefit from the purchased power in any way other than what was contemplated by the parties at the time of contracting.

Instead, Alcoa used the power that it purchased to continue operating its aluminum smelting facility for its own benefit. Alcoa would have been required to obtain such a power supply in any case in order to accomplish that objective. Entering into the Amendment allowed Alcoa to purchase its power at a price that was below the market price at which it was purchased. As a result, Alcoa's contractual expectations were fully realized and it suffered no cognizable injury. The purpose of equity is to preserve a party's rightful position, not to allow him to revise history and rewrite the contract from top to bottom as he chooses.

Bonneville hopes that its decision in this case renders further discussion of these contentious issues purely academic. That aside, as discussed below, Bonneville does give more credence to the view that many of Alcoa's arguments would further detract from Bonneville's ability to recover the $25.6 million if interposed as a defense, counterclaim, or offset to damages.

c) **Evaluation of Alcoa's Claim as a Potential Defense and/or Counterclaim.**

PPC states that "BPA concluded in the Draft ROD that the [Alcoa] counterclaim 'has no merit." PPC at 2-3. PPC reasons that, as a consequence, Alcoa has no counterclaims that could influence BPA's decision whether to pursue a recovery or not.

It is apparent that either PPC has misinterpreted BPA's position or Bonneville was not sufficiently clear in the DROD. In the DROD, BPA attempted to distinguish between the strength of Alcoa's arguments as affirmative claims against BPA, as opposed to the strength of Alcoa's arguments as counterclaims or defenses to an action initiated by BPA. BPA concluded that, as affirmative claims, Alcoa's arguments would have little merit, but that its arguments would likely carry more weight as counterclaims or defenses to any claim BPA might bring. In the DROD, Bonneville did not address the latter issue thoroughly, in part, due to the way the Court had framed its remand order and, in part, due to BPA's reluctance to argue a potentially adverse litigant's defensive posture for him, as opposed to being critical of his affirmative adverse claim. The distinction, however, is important, especially given the fact that this case does not involve a breach of contract and therefore any claim Bonneville might bring against Alcoa would likely be an equitable claim where the various defenses interposed by Alcoa would necessarily require the court to engage in balancing the equities of the situation as a whole.

In that vein, Bonneville's conclusion that Alcoa did nothing fraudulent, negligent, or otherwise improper to obtain the payment remains an important issue, regardless of whether it is analyzed in terms of mistake, illegality, or unjust enrichment, or weighed in the context of a defense grounded in implied in fact contract, *quantum valebant*, or estoppel based on material reliance. For instance, if BPA sought disgorgement of the amounts paid to Alcoa on a theory of unjust enrichment, a court would necessarily consider all the factors that pertain to Bonneville's claim, including the damages that Alcoa allegedly incurred, the extent to which BPA was responsible for any mistaken legal understandings, Alcoa's malfeasance or lack thereof, and the extent to which Alcoa was induced to materially rely on the terms of the contract.

Further, while the difficulty of working an estoppel against the government is widely recognized, in this case, the Alcoa Amendment explicitly acknowledges Alcoa's material reliance on Bonneville's payments and on the Administrator's understanding of the law at the time of contracting, which later proved to be mistaken:

> In reliance on the payments to be made to it by BPA under the Agreement, Alcoa acquired power in the wholesale power market to serve its industrial load during the full term of the Agreement. . . . BPA understands the December Opinion to prohibit payments by BPA to Alcoa that would exceed the difference between the Industrial Firm Power (IP) rate, and BPA's forecasted wholesale market price.

Due to this language, Bonneville believes that Alcoa has a more tenable basis to argue reasonable material reliance than presented in the cases cited by PPC, including such cases as *Independent School District* and *Old Republic*.

To be clear, Bonneville still believes that, were Alcoa to make its claim affirmatively, rather than defensively, it would face challenges equal to or greater than Bonneville would face mounting an affirmative claim. The long and short of it is that, in this instance, both parties essentially got what they bargained for and there is no injustice on either side for which the court would likely be inclined to craft an equitable remedy. If

Alcoa initiated a case against Bonneville, in all likelihood Bonneville could successfully defend the case. The same is true in reverse. Alcoa could point to the facts that it lays out in its comments to show that Bonneville was not the only party adversely affected by the transaction, and the court would probably be inclined to agree that Bonneville is not entitled to equitable relief under the principles analyzed herein.

Therefore, Bonneville disagrees with PPC's assessment that a claim for recovery of funds spent pursuant to the Amendment could be successfully prosecuted based on the common law. To the contrary, regardless of which legal theory is being espoused, Bonneville's view of the case law suggests that, in circumstances such as this, the courts are reluctant to deprive those who contract with the government of the benefit of the bargain they have obtained where they have done nothing improper to obtain it. Thus, Bonneville cannot, as suggested by PPC, ignore the possibility that Alcoa could successfully demonstrate that it would not be fair or equitable to require disgorging the amounts paid under the Amendment, regardless of the Ninth Circuit's later opinion that the payments were not consistent with sound business principles.

Moreover, Bonneville is vested with broad authority to contract for the sale of power in much the same manner as a private business concern. Despite the copious case law cited by both parties and by Bonneville—in support of or against one proposition or another—Bonneville's status as an actor in the stream of commerce cannot be ignored when evaluating the legal risk associated with initiating litigation. There is every reason to believe a court would simply view this as an arm's length transaction between two sophisticated parties who understood the transactional risks and accepted them. It is highly unlikely that a reviewing court would resort to equitable principles to relieve Bonneville from the consequences of its own business decisions, particularly when, as discussed below, the subsequent course of dealing was highly favorable to Bonneville's business interests.

D. Whether, in Light of the Totality of the Circumstances, Bonneville Should Pursue Recovery Efforts

Bonneville appreciates the time and effort spent by interested parties providing their perspectives and opinions on the issue to be addressed at this time, *i.e.*, whether BPA will initiate efforts to recover approximately $25.6 million spent pursuant to the Alcoa Amendment, which was put in place after the Ninth Circuit's decision in *PNGC I.* The Administrator understands that there are multiple interests at stake and his purpose here is not to simply weigh the respective monetary value of those interests or, in essence, to declare winners and losers in this situation. As noted by PPC's comments in a section titled "Pertinent Business Considerations,"

> Instead of making the decision on remand in isolation, the Administrator should consider whether to pursue recovery of BPA's unlawful payments to Alcoa in the context of the agency's broader mission to provide low-cost power and the agency's recent commitments to control its costs, preserve the value of the federal

system, and be competitive in 2028 when the current Regional Dialogue power contracts terminate.

PPC comments at 6. Bonneville echoes the sentiment expressed by its preference customers. That context begins with the Administrator's belief that at the time the Administrator entered into the Alcoa Block Power Sale Contract, and the subsequent Alcoa Amendment, providing service to Alcoa would lead to long term economic stability within the Pacific Northwest and help keep Bonneville's wholesale power rates low. It includes subsequent legal challenges to those transactions and the resulting court opinions as well as Bonneville's efforts to respond to the defects identified by the Court. The results of those efforts also provide part of the context for Bonneville's consideration. At this juncture, the Administrator's role is essentially to consider all competing interests and at the same time reach a sound conclusion that he believes best serves the interests of the Bonneville Power Administration and the Pacific Northwest region over the long term. This section discusses the Administrator's decision-making process and the context in which his final decision not to pursue recovery efforts was made.

One major purpose of the Alcoa Amendment was to preserve the status quo while fully considering the implications of the *PNGC I* decision. The Administrator conformed the Amendment to the Ninth Circuit's view that DSI sales must be based on the IP rate but monetized arrangements were not prohibited by the order. The Administrator believed further that such a transitional period, or bridge, was necessary. It would allow Bonneville sufficient time to conduct necessary internal and public processes in order to make a final determination regarding how best to move forward in light of the Court's decision that the original DSI Block Sales contracts were not consistent with sound business principles. The Court's decision, in the Administrator's view, was not intended to prohibit, or even discourage, the Administrator from conducting business with one of its historical customer classes. It did, however, make clear that in the future Bonneville would need to assure that doing business with DSI customers, in the long term, was based on a more narrow view of what is required to assure that such sales are consistent with Bonneville's business interests, rather than the economic interests of the region more generally.

To assure that Bonneville made appropriate additional adjustments to comply with the Court's opinion, Bonneville developed the Equivalent Benefits Test to assess whether any future contract offers would provide tangible financial benefits equal to or greater than those that would be achieved by adopting the most likely alternative of selling the same power at prevailing market prices. That effort was sustained by the Court and, it should be noted, has been successful in achieving financial benefits, as shown more specifically below, that exceed even those that were originally forecast by the Equivalent Benefits Test.

In its DSI Lookback deliberations, Bonneville also determined that it would not seek recovery of funds expended either pursuant to the Block Sales Contract or the later Alcoa Amendment. In the former case, Bonneville's determination was based on the inclusion

of a damage waiver provision in the contract. That provision and Bonneville's decision that it precluded any recovery efforts were sustained by the Court. While the damage waiver was absent in the Alcoa Amendment, for a number of reasons, Bonneville also decided that it would not seek recovery of those amounts either. In its remand opinion, the Ninth Circuit concluded that the record before the court was not adequate to support the decision not to pursue recovery of funds spent pursuant to the Amendment.

That is the sole issue remaining after many years of complex litigation involving multiple issues surrounding DSI service. Thus, the Administrator is now essentially called upon to revisit the facts and circumstances surrounding the narrow issue of the Alcoa Amendment and decide whether to initiate actions aimed at recovering amounts spent in connection with the Amendment or to forego any such recovery efforts.

Preference customers have strongly advocated pursuing recovery of the amounts spent pursuant to the Amendment. They have cited many court cases and other materials in support of that view. Their research and work here is appreciated. Bonneville has examined that analysis thoroughly in previous sections of this ROD. At this time, it is important to underscore Bonneville's belief that the cases cited by PPC are not analogous to the actions taken in this case by Bonneville. For the most part, the cases cited by PPC pertain to actions taken by agents of the government that were contrary to existing regulations. In contrast, at the time the Administrator exercised his authority to contract with Alcoa in the manner that he did, his actions were based on a good faith belief that his actions were consistent with the law, as determined by the Court in a subsequent opinion. Thus, only upon later legal challenge did the court find the Administrator exceeded his authority. That distinguishing factor is fundamental to Bonneville's conclusion that any pursuit of the recovery effort advocated by preference customers would require the commencement of, not simply a collection effort, but some type of formal legal action by Bonneville. With that assumption in mind, the Administrator has considered all of the information available to him at this time, including the analysis provided elsewhere in this ROD evaluating other discrete issues identified by the Court.

In addition to that analysis, the Administrator also has turned for general guidance to specific statutory provisions governing the initiation of litigation. Section 832k(b) of the Bonneville Project Act of 1937 provides in part:

> The Administrator may, in the name of the United States, under the supervision of the Attorney General, bring such suits at law or in equity as in his judgment may be necessary to carry out the purpose of this chapter.

16 U.S.C. Sect. 12(b). This provision provides statutory authorization for initiating litigation such as that urged by the preference customers, but it is important to underscore that it is not the Administrator's decision alone. Instead, any litigation to pursue recovery must be supported by and conducted under the supervision of the Attorney General or U.S. Department of Justice acting on his or her behalf. Thus, in no small measure, the Administrator's view of when to invoke the authorization to bring legal action is tempered by an institutional understanding of what that process requires and, more

importantly, when it is appropriate to make a request to use governmental legal resources in pursuit of a claim and when it is not.

Moreover, because the situation here involves a contract entered into by the Administrator with a member of a customer class identified by statute, the Administrator has also turned, for additional general guidance, to statutory provisions governing his contracting authority. Section 2(f) of the Bonneville Project Act of 1937 provides:

> Subject only to the provisions of this chapter, the Administrator is authorized to enter into such contracts, agreements, and arrangements, including the amendment, modification, adjustment, or cancellation thereof and the compromise or final settlement of any claim arising thereunder, and to make such expenditures, upon such terms and conditions and in such manner as he may deem necessary.

16 U.S.C. Section 832a(f).

As noted elsewhere in this document, considerable time was provided, with Bonneville's full support, to give parties with a direct interest in this matter sufficient time to explore the possibility of reaching a settlement or compromise that would make further efforts on this matter unnecessary. The Administrator regrets that such efforts failed to yield positive results. As a result, in addition to exercising his judgment with respect to whether pursuing recovery of monies expended is necessary to further Bonneville's responsibilities, the Administrator is left, in the absence of compromise and settlement, to make a determination regarding what constitutes a fair and reasonable final resolution of claims arising from the Alcoa Amendment.

In total, these basic statutory provisions make it clear that the choice is fundamentally a question of the Administrator exercising his sound judgment as to what action best serves Bonneville's policies and business interests, consistent with legislative provisions governing Bonneville's activities.

To review, as a first step in the decision-making process Bonneville reduced to a sum certain the amount spent in conjunction with the Amendment. As noted elsewhere, that amount has been reduced to a sum of approximately $25.6 million.

A necessary second step was to conduct a legal risk assessment that identified and analyzed various potential avenues of recovery as directed by the court. That assessment concluded that legal efforts to pursue recovery of payments made under the Amendment would not be likely to lead to a successful outcome. Generally speaking, the analysis concluded that legal rules governing the potential legal theories do not support recovery efforts. In that regard, the Administrator has been advised that certain policy exceptions to the prevailing rules exist, but such exceptions are limited and not frequently successful. Moreover, the analysis concludes that in most instances where an exception could be invoked, other competing policy considerations could well compel an

unfavorable outcome, not the least of which is upholding the sanctity of contracts entered into in the stream of commerce by knowledgeable parties.

The Administrator was also advised that, in some instances, Bonneville would be required to show that Alcoa engaged in some kind of affirmative misconduct like fraud, duress, or misrepresentation in order to sustain a claim for return of the money. Bringing such a claim would not be appropriate in this instance because there was no such conduct by Alcoa and on the contrary, the Amendment was a contract produced through arm's length negotiation based on the Administrator's understanding of the law at the time the contract was made.

Bonneville's legal analysis does not give much credence to Alcoa's alleged claims against Bonneville; it does nonetheless view Alcoa's position, on the whole, has having a negative impact on Bonneville's probability of achieving a successful outcome. Additional analysis is provided in this ROD examining Alcoa's claim as a counterclaim or defense, as opposed to an affirmative claim. Based on that analysis, the Administrator concludes that any collection would be further undermined by the prospect that Alcoa could successfully defend, in whole or in part, against a claim for recovery of the $25.6 million.

In short, the Administrator concludes that, based on the analysis, pursuing legal action to recover amounts expended under the Amendment would be a very doubtful proposition. Adopting such a strategy would not, in the Administrator's judgment, be a reasonable course of action. Put differently, the Administrator cannot recommend to the Department of Justice that it undertake a litigation effort that he believes does not show much promise of leading to a favorable outcome.

With respect to determining, as a matter of contract administration, how this matter should be resolved, the Administrator has also considered that both parties to the Block Sales Contract and the subsequent Alcoa Amendment incurred significant costs due to the Court's unfavorable view of those transactions. From a contract administration standpoint, Bonneville views those costs fundamentally as transactional financial risks that should be borne by both parties to the contract. Bonneville has a great deal of flexibility to operate as a business, consistent with its statutory authorities. The Court recognizes as much and has noted that the Administrator is often faced with trying to reconcile competing interests and has good reason, at times, to test the limits of Bonneville's statutory authority when entering into contractual relationships.

In the context of offering to sell power to the DSIs, legal risk has been inherent in such transactions at least since the termination of Bonneville's long-term power sales contracts with the DSIs in 2001. In response to the *PNGC I* and *PNGC II* opinions, subsequent DSI contracts have been based on a different set of considerations, embodied in the Equivalent Benefits Test. The first of those contracts was challenged in the Ninth Circuit, both by Alcoa and the preference customers, and was upheld. In any case, recognition of legal risk in the area of DSI contracting has been the rule, rather than the

exception, for many years and the Block Sales Contract and Amendment were not exceptional in that regard.

From the standpoint of preference customer interests, the Administrator recognizes that, when costs are incurred on a transactional basis, those costs must be recovered in customer rates. PPC makes note of this fact, among others, in its comments:

> PPC and PNGC have consistently urged the Administrator to take all reasonable actions to reduce its costs because BPA's power customers cannot absorb the steep trajectory of BPA's rates. A few months ago, the Administrator raised the power rates by another 7.1% on average, which came on the heels of substantial rate increases in each of the last two rate periods. . . .BPA's approach to its ultimate decision in this matter should be focused on the business interests of BPA and its preference customers, who have borne the costs of BPA's unlawful payments to Alcoa.

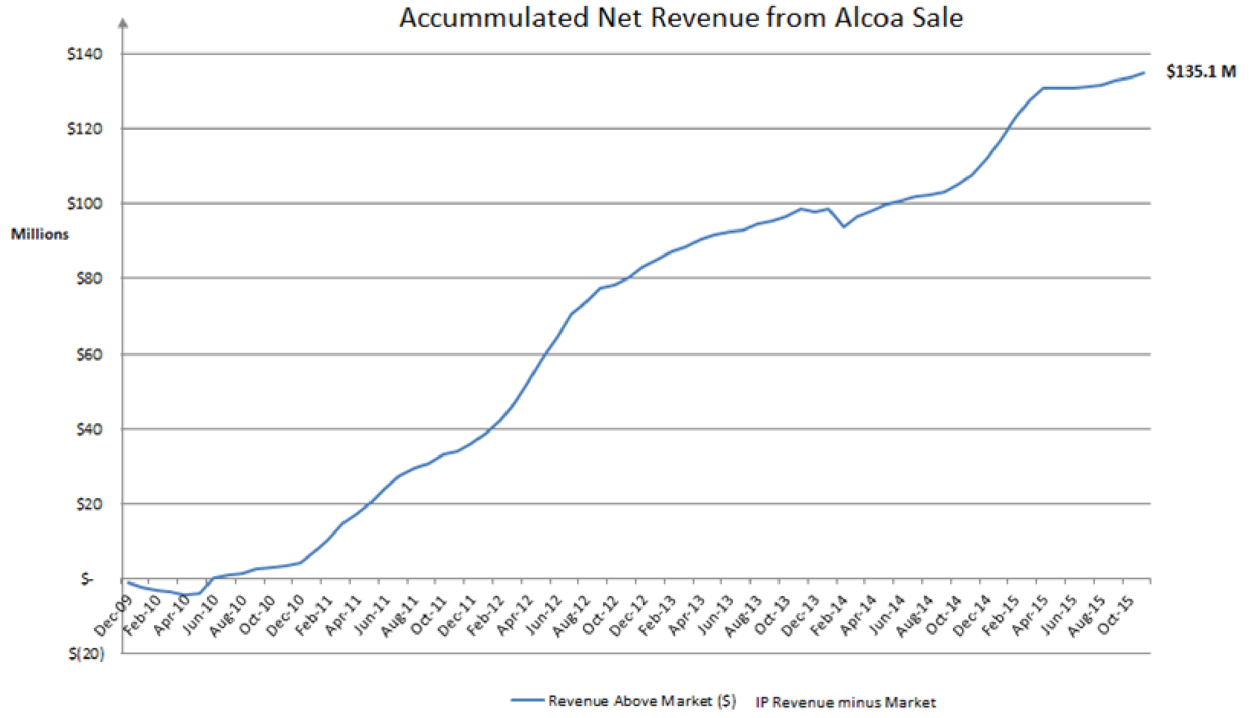
PPC Comments at 6-7. For present purposes, the Administrator makes two points. First, on the whole, doing business with Alcoa over the long term has had a positive impact on all customer rates for reasons that have been articulated many times, not the least of which is a guaranteed revenue stream at a rate that often reflects a higher price than could be obtained in the market. This has been particularly true in recent years, when low gas prices, also noted by PPC, have had the effect of creating lower wholesale prices for electricity in the markets to which Bonneville has access for its secondary sales of surplus power.

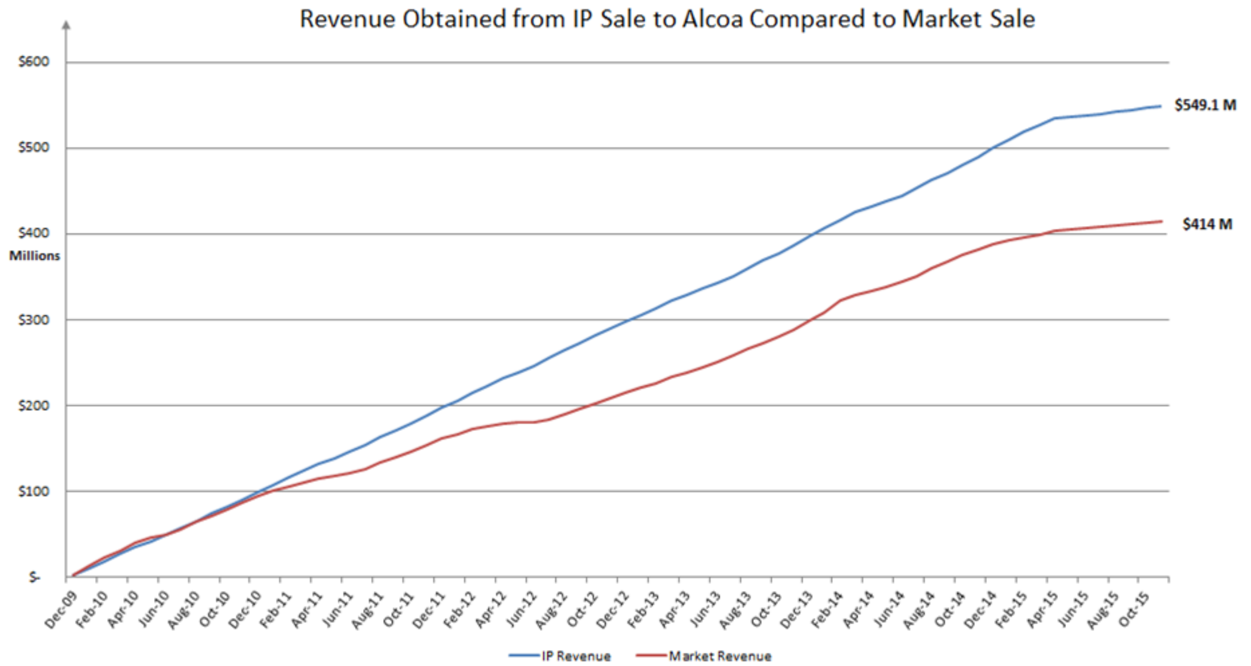
Second, all of Bonneville's customers have placed a high priority on the Administrator's contracting flexibility and his ability to use that flexibility to find solutions to the myriad issues that confront the agency on a daily basis. Customers have, in the past, almost uniformly supported the policy of Bonneville standing behind its contracts once they are entered into and performed in whole or in part. The Administrator sees no reason to deviate from that approach, especially when attempting to do so would result in protracted litigation with a low probability of success.

A related issue considered by the Administrator with respect to contract administration is the course of conduct of the parties in the atmosphere of legal risk noted above, and in the wake of the adverse *PNGC I* and *PNGC II* opinions. In that context, both Alcoa and Bonneville exhibited a pattern of working together through negotiation, rather than litigation, to comply with the opinions and resolve differences in a manner that promoted maintaining and continuing a mutually beneficial business relationship. That relationship continues to this day and in recent years, as noted above, has resulted in a revenue stream for Bonneville that has exceeded the revenues that would have been generated by selling the same power into the market.

Bonneville's analysis shows that, based on the same metrics employed by the Equivalent Benefits Test, Bonneville has achieved $133 million in net revenues (*i.e.*, the difference between the IP rate and prevailing market prices) since payments under the Alcoa

Amendment terminated. As shown below, that figure is well above the revenues projected under the EBT analysis:





It should be noted that the net revenue evaluation does not include other tangible benefits included in the EBT analysis*, e.g.,* operating reserves and decreased transmission costs. Thus, this subsequent course of dealing ultimately provided net financial benefits to both Bonneville and its power customers, particularly preference customers, by mitigating rate increases and/or lowering the level of Bonneville's wholesale firm power rates.

The Administrator appreciates all of the comments received and takes note especially of the thorough and highly nuanced legal analysis provided in that connection. After fully considering all of the arguments advanced as part of this process, it is necessary to step back from the technical arguments, as anyone who is not a legal expert must do, and look at this situation from a principled and pragmatic business perspective. Here, that includes weighing the long term benefits that accrued to Bonneville and its preference customers as a result of BPA's effort to keep future business opportunities open by entering into the Amendment and subsequently developing the EBT to assess subsequent transactions:

1. During the Amendment period Bonneville expended $25.6 million, which kept Bonneville out of the unpredictable power market and provided a bridge to future contracts that could potentially provide financial benefits to Bonneville in return.

2. Bonneville entered into several contracts and amendments based on its expectation, as projected by the Equivalent Benefits Test, that financial benefits would be forthcoming.

3. Bonneville's current economic analysis shows that Bonneville achieved financial and other benefits well in excess of the value that it expected to receive pursuant to the EBT analysis and far beyond the $25.6 million spent pursuant to the terms of the Amendment.

From a business standpoint, Bonneville's contracts with Alcoa since the *PNGC I* opinion have made good business sense, and it would not be good policy, at this point, for the Administrator to disregard the positive end of the bargain in those instances when Bonneville reaped an upside only to disclaim any responsibility for the contractual risk in the one instance when there was a comparatively small downside.

Finally, it is worth noting, as an aside if nothing else, that Bonneville has been serving direct service industrial load since the 1930s. Historically, DSIs, including Alcoa, have been valuable customers on many levels, including the fact that the load served by Bonneville remained sufficiently diversified so as to create more financial and operational flexibility, not less. Alcoa is Bonneville's sole remaining large industrial customer and has continued to provide power reserves and has been active in Bonneville's demand response program. This type of direct system benefit has been a part of the historical cooperation that has contributed over time to maximizing the value of the Federal Columbia River Power System for everyone in the Pacific Northwest region.

E. Conclusion

In conclusion, litigation regarding DSI service, in one form or another, has been ongoing virtually without interruption for well over a decade. In light of the low probability of a positive legal outcome, the Administrator does not see any significant benefit from its continuation over expenditures that have been exceeded by the benefits derived from Alcoa contracts entered into subsequent to the *PNGC I* and *II* opinions. It is true that Bonneville's contracts with DSI customers and Alcoa in particular, have sometimes, over the course of its seventy-five year history, had a downside for Bonneville on a transactional basis. More frequently, they have resulted in an upside, providing over an extended time frame substantial financial and operational benefits. In order to practice sound business principles, the Administrator must take a long term view of the value of business relationships, rather than focusing on a narrow window of time where a considered business decision resulted in a short term loss but ended up preserving the longer term benefits associated with subsequent transactions. The Administrator is satisfied that Bonneville's business relationship with Alcoa has been a positive one and initiating a further round of protracted litigation would be unproductive.

/s/ Elliot E. Mainzer January 21, 2016

Elliot E. Mainzer
Administrator and Chief Executive Officer
Bonneville Power Administration