BONNEVILLE POWER ADMINISTRATION DRAFT 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 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 BPA's conclusions with respect to the Alcoa Amendment, Bonneville requested commenters to provide any legal arguments they believe support their respective positions that Bonneville should or should not pursue a recovery of benefits.

This Draft Record of Decision (DROD) responds to the questions posed by the court and comments made thus far. Interested parties are invited to provide additional comments by October 9, 2015.

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

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 attempt 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 argues 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 argues 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.

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 draft conclusion is 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 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 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, not the amount the preference customers might allege as the total amount they believe should be recovered from Alcoa. Therefore, Bonneville has not revised its estimate to account for this alleged post-termination interest expense.

Based on these comments, 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>

In their comments, Bonneville's preference customers urge Bonneville to be creative in evaluating alternative paths for recovery and not restrict itself to traditional legal avenues. PPC Comments at 1-2. Their concern is 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 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 Comments at 2-6.

In contrast, Alcoa argues that it is the party injured by the Alcoa Amendment. According to Alcoa, it suffered substantial losses related to purchased power costs 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

contends that if Bonneville had offered a physical power sale at the IP rate, Alcoa would have suffered no 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.

As a result of the Court's directives in *ICNU*, and after considering the above 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 law; (4) unjust enrichment, and (5) administrative offset. Each avenue is assessed to determine whether there is a reasonable probability of obtaining recovery of all or part of the $25.6 million.

However, before addressing these legal theories, it should be noted that efforts were made to resolve this matter informally by agreement 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 to be consummated in a manner that allowed Bonneville to avoid the risk of possibly buying power from the market at fluctuating prices to fulfill its obligation. This construct essentially hedged Bonneville's risk of having to acquire

power from the market at fluctuating power prices and achieved certainty with respect to Bonneville's financial risk. That risk was a concern raised by preference customers in public discussions regarding service to DSI customers held prior to Bonneville's decision to offer monetized power sales contracts to Bonneville's then remaining DSI customers. *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 in the wholesale power market. Ultimately, Alcoa accepted the offer.

The Administrator's draft 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.
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> 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 would likely not succeed in this case.

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 that 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. On the one hand, 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, even when the legal authority to enter into the contract was in question.

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* and *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," 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 prospective 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 of payments made pursuant to the Alcoa Amendment. However, Bonneville's draft 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 next 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 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 is 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.
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> 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 render the Alcoa Amendment subject to rescission. Thus, the doctrine of mistake of law would provide no 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, where Bonneville is the party charged with responsibility for interpreting the statutes that govern its activities, it could be argued that any mistake of law was primarily due to Bonneville's mistake of law rather than the mutual mistake of Bonneville and Alcoa. Indeed, Alcoa has made this argument, and to be clear, Bonneville disagrees with many aspects of Alcoa's argument. However, a court might 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 draft 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 of monies expended in connection with the Alcoa Amendment 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.
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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 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. Nor would such an abrupt change to a physical power sale have been particularly advantageous to Alcoa at the time of the Alcoa Amendment. To support a transaction of only twelve months duration, Alcoa 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 power supplied directly by Bonneville.

Thus, 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 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 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.

As a result, Bonneville's draft determination is that 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 an express contract that was 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 draft 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 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 the government (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 draft 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 BPA 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. BPA can only comprehensively address the issues that are now before it in this proceeding.

Suffice it to say that, 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 and 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 complete termination of its previous 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 BPA and create a potential result that would not only render such ratemaking efforts irrelevant, but also result in lost revenue.

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 Comments at 17. BPA agrees that presently BPA has 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.

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 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. <u>Legal Status of the Block Sale Contract Damage Waiver Provision</u>

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 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 period. This 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 these 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 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, especially following issuance of *PNGC I*, it was clear that service to Alcoa was discretionary. 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. 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 those 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—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 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.

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 claim of damages is not viable and would not prevail.

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

Alcoa's comments go on to 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 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. The existence of these express contracts totally negates the idea that an implied in fact contract could also exist governing the same subject matter.

Nevertheless, in support of this implied in fact theory, Alcoa points to statements made elsewhere that, had Bonneville known the Ninth Circuit would find the monetized construct of the Block Sale Contract defective, the parties could have negotiated some

other arrangement to provide power in a way that promotes widespread use, at the lowest rates possible, consistent with sound business principles. Such hindsight, however, hardly gives rise to a "mutuality of intent to contract" under different terms and conditions. At the time of contracting, there was a mutual intent to contract, but Bonneville was unwilling to offer a physical power sale at the IP rate. The fact that Alcoa may have preferred such a sale is not relevant to showing that there existed a mutuality of intent to contract on that basis. On the contrary, the existence of the express contract, the Block Sale Contract, without those terms and conditions, demonstrates precisely the opposite.

More significantly, as noted, the law is clear that the Administrator is authorized but not required to offer power sales contracts to a DSI. Because Bonneville did not make an offer other than the Block Sale Contract and Alcoa Amendment, there was no other offer for Alcoa to accept, thus answering the question of whether the offer and acceptance was "unambiguous." The express contracts were agreements that provided Alcoa offsetting payments for its purchased power costs. In exchange, Bonneville avoided the market risk associated with unpredictable costs it might have otherwise incurred. Alcoa's theory is pure conjecture and it is essentially an attempt to require Bonneville to indemnify Alcoa for supposed "costs" it allegedly incurred under a contract that never existed and was never even contemplated at the time of contracting.

Suffice it to say that, on every level, both parties entered into the Block Sale Contract and Alcoa Amendment based on their own considerations, business or otherwise, and both received 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.

BPA's draft determination is that Alcoa's claim has no merit.

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

This Draft ROD describes BPA's progress in addressing the issues remanded by the Court and invites further input on this process. To summarize:

1. **Amount Paid under the Amendment.** The amount expended pursuant to the Alcoa Amendment is $25,627,143.95, or rounded to approximately $2.6 million for convenience. The comments did not convey any significant disagreement with Bonneville's assessment.

2. **Potential Avenues of Recovery**. To support and further this decision making process, Bonneville has provided a draft legal risk assessment that identifies and

analyzes various potential avenues of recovery as directed by the court. At this point, that assessment indicates that the legal rules governing the potential legal theories do not support a favorable outcome.

The analysis notes further that certain policy exceptions to the prevailing rules exist, but such exceptions are limited and are not often successful. Moreover, in most instances where an exception could potentially be invoked, competing policy considerations must be considered in assessing the probability of achieving a recovery. In other instances, Bonneville would be required to show that Alcoa engaged in some kind of affirmative misconduct like fraud, duress, or misrepresentation in order to succeed in any recovery effort, which would be extremely difficult in the context of an arm's length commercial transaction.

3. **Analysis of Alcoa's Claim**. At this time, the legal analysis does not give much credence to Alcoa's alleged claims against Bonneville as an affirmative claim, but it does nonetheless view Alcoa's position, on the whole, as having a negative effect on Bonneville's chances of ultimately demonstrating that Alcoa was unjustly enriched or otherwise showing that the Amendment payments made by Bonneville should be disgorged.

Bonneville welcomes and encourages further comment on all of these issues.

Additionally, the fourth issue identified by the Court is for Bonneville to "either adopt one of those plans [for recovery of funds spent pursuant to the Amendment] or to explain why, with respect to each of them, the costs and downside risks justify abandonment of the opportunity to recover any overpayment." As noted above, the legal analysis for Bonneville's draft decision whether to pursue a recovery of funds, or not, are incorporated into the analysis of the second and third issues. However, at this juncture, Bonneville has not yet reached a final determination and commenters are encouraged to provide any additional input, legal or otherwise, that might assist the Administrator in making his final decision.