

**UNITED STATES OF AMERICA
U.S. DEPARTMENT OF ENERGY
BEFORE THE
BONNEVILLE POWER ADMINISTRATION**

**2007 SUPPLEMENTAL WHOLESALE)
POWER RATE ADJUSTMENT PROCEEDING) BPA DOCKET WP-07 SUPP
_____)**

**LEGAL MEMORANDUM OF THE
IDAHO PUBLIC UTILITIES COMMISSION**

The Bonneville Power Administration (BPA) has no express legal authority to engage in retroactive ratemaking or provide retroactive relief in this proceeding. Consistent with its authority in Section 7 of the Northwest Power Act, BPA should only set rates prospectively. The successful petitioners in the two circuit appeals failed to avail themselves of established stay procedures and thus should only be accorded prospective relief. In addition, the deemer accounting mechanism is not authorized by the Northwest Power Act and deemer balances should not be included in the “Lookback” mechanism. Consequently, the Administrator should reject the Lookback mechanism as unlawful, arbitrary, and not in conformance with sound ratemaking principles.

BACKGROUND

A. The Ninth Circuit Opinions

On May 3, 2007, the United States Court of Appeals for the Ninth Circuit issued two opinions in consolidated appeals challenging BPA’s Residential Exchange Program (REP) Settlement Agreements and certain rates in BPA’s WP-02 Wholesale Rate proceeding. In *Portland General Electric Co. v. Bonneville Power Admin.*, 501 F.3d 1009 (9th Cir. 2007) (“*PGE*”), the Court held that BPA’s REP Settlement Agreements with the six regional investor-

owned utilities (IOUs) were contrary to the Northwest Power Act, 16 U.S.C. §§ 839-839h. The Court also held that BPA improperly included these “settlement costs” in the rates paid by preference customers in violation of Section 7(b)(2) and (3) of the Northwest Power Act, 16 U.S.C. § 839e(b)(2) and (3). *PGE*, 501 F.3d at 1036. The Court held “that BPA was bound by the power exchange requirements of the [NPA], and that BPA exercised its settlement authority contrary to those requirements.” *Id.* at 1013. It granted the petitions for review.

In the companion appeal, *Golden Northwest Aluminum, Inc. v. Bonneville Power Admin.*, 501 F.3d 1037 (9th Cir. 2007) (“*Golden Northwest*”), three groups of petitioners also challenged BPA’s WP-02 preference power rates. Two groups argued that the established preference rates were too high. More specifically, the first group asserted that BPA inappropriately allocated the costs of supplying power to the DSIs to the preference rates. The second group insisted that BPA erroneously allocated REP settlement costs to the preference rates. The Ninth Circuit held against the first group but held for the second group. *Golden Northwest*, 501 F.3d at 1040-41. In granting the petition of the second group, the Court stated that the holding in *PGE* was dispositive in this case: BPA improperly allocated the costs of the REP settlement agreements in the rate paid by preference customers. *Id.*, at 1048.

The third group of petitioners argued the preference rates were too low for BPA to meet its fish and wildlife obligations. The Court agreed. *Id.*, at 1052-53. The Court “therefore remand[ed] to BPA to set rates in accordance with this opinion.” *Id.* at 1053 (emphasis added).¹ On October 5, 2007, the Court denied petitions seeking rehearing and *en banc* on the two opinions.

¹ Several of the IOU parties in the two appeals have filed a joint Petition for Certiorari with the United States Supreme Court. _____ U.S.L.W. _____ (U.S. Feb. 7, 2008) (No. 07-1007).

B. Remand to BPA

Following the two Circuit opinions, BPA suspended REP payments to the IOUs effective June 2007. BPA later acknowledged “the Ninth Circuit provided little guidance to BPA in its [two] decisions regarding the subsequent actions BPA should take in response to those opinions.” BPA Response to APAC’s Motion to Strike, WP-07-M-BPA-77 at 5. Settlement negotiations were unsuccessful and BPA subsequently issued its Federal Register Notice re-opening this WP-07 case. 73 Fed.Reg. 7,539 (Feb. 8, 2008). Because BPA’s WP-07 proceeding used the same methodology that the Court overturned in the WP-02 proceeding, BPA’s response to the opinions² is to “correct both the WP-02 rates and the WP-07 rates and response to the Court’s rulings.” WP-07-E-BPA-52, p. 2, line 14.

ARGUMENT

A. BPA Cannot Correct the WP-02 Rates

Despite BPA’s intent to correct the WP-02 rates, these rates have been superseded. Indeed, the WP-02 rate period ended September 30, 2006. In fact, on September 21, 2006 the Federal Energy Regulatory Commission (FERC) granted interim approval of BPA’s new WP-07 rates effective October 1, 2006 (subject to refund). *Order Approving Rates on an Interim Basis and Providing Opportunity for Additional Comments*, Docket No. EF06-2011-000, 116 F.E.R.C. Rec. ¶ 61,264 (Sept. 21, 2006). The WP-07 rates currently remain in effect pending completion of this supplement proceeding and final FERC approval. On March 4, 2008, BPA moved FERC to continue the previously granted Stay of the WP-07 rates through September 4, 2008.

As the chronology above clearly demonstrates, the WP-02 rates no longer exist because they have been superseded by the interim WP-07 rates as of October 1, 2006. The only

² In October 2007, the Ninth Circuit also issued a third opinion addressing the 2004 amendments to the REP Settlement Agreements. *Public Utility Dist. No. 1 of Snohomish Cty, Wash. v. Bonneville Power Admin.*, 506 F.3d 1145 (9th Cir. 2007).

“retroactive” relief that the consumer-owned utilities (COUs) may be entitled to is the “refund with interest” of the interim WP-07 rates if these interim rates are determined to be too high. 18 C.F.R. § 300.20(c); *see also* 18 C.F.R. § 300.21(g) (“if a rate collected by any power marketing administration on an interim basis exceeds the rate which is confirmed and approved by [FERC] as a final rate, the Administrator . . . must refund with interest any rate collected during the interim period which exceeds the final rate.”). Thus, BPA cannot correct the WP-02 rates.

B. The Court Did Not Order BPA to Provide Retroactive Relief

There is nothing in the Ninth Circuit’s two decisions that requires BPA to provide retroactive relief to the prevailing parties in the *PGE* and *Golden Northwest* cases. In *Golden Northwest* the Court “remand[ed] to BPA to set rates in accordance with this opinion.” 501 F.3d at 1053. BPA has re-opened the WP-07 proceeding with its interim rates still in effect. Because BPA has requested an extension of the existing stay of the WP-07 interim rates, BPA should simply proceed to set lawful rates.

In neither case did the Ninth Circuit vacate the BPA rates. Indeed, given the Court’s findings in *Golden Northwest* that the rates were both too high and too low, the Court remanded the matter back to BPA “to set rates in accordance with this opinion.” *Id.* This is consistent with the well-established rule that Courts do not set rates – they are empowered to set aside agency action. 5 U.S.C. § 706(2). It is BPA that is vested with the authority to “establish, and periodically review and revise, rates for the sale and disposition of electric energy and capacity” Section 7(a)(1), 16 U.S.C. § 839e(a)(1). Moreover, it is for BPA to first establish rates and then submit those rates for “confirmation and approval by” FERC. Section 7(a)(2), 16 U.S.C. § 839e(a)(2).

***C. BPA has no Statutory Authority to Engage in
Retroactive Ratemaking or Provide Retroactive Relief***

The law is clear: a federal agency must have express statutory authority before it can engage in retroactive ratemaking or provide a retroactive remedy such as reparations or refunds. In *Bowen v. Georgetown University Hospital*, 488 U.S. 204, 109 S.Ct 468, 102 L.Ed.2d 493 (1988), the United States Supreme Court declared that “[r]etroactivity is not favored in the law. Thus, congressional enactments and administrative rules will not be construed to have retroactive effect unless their language requires this result.” 488 U.S. at 208, 109 S.Ct at 471. Indeed, because it is not a sound business practice to retroactively increase rates, the Court requires that Congress expressly permits such a practice in no uncertain terms. *Bowen*, 488 U.S. at 208, 109 S.Ct. at 472. “The power to require re-adjustments for the past is drastic. It . . . ought not to be extended so as to permit unreasonably harsh action without very plain words.” *Id.*, quoting *Brimstone R. Co. v. United States*, 276 U.S. 104, 122, 48 S.Ct. 282, 287, 72 L.Ed. 487 (1928). IOU customers are not a fungible mass where future customers may be substituted for past customers to make up for past rate deficiencies. *Utah Power & Light Co. v. Idaho Public Utilities Commission*, 685 P.2d 276, 285 (Idaho 1984).

There is no authority in Section 7 of the Northwest Power Act which expressly permits BPA to engage in retroactive ratemaking. On the contrary, the ratemaking scheme embodied in Section 7 contemplates that rates will be set prospectively. In particular, the Administrator shall establish rates and such rates shall be “revised to recover, in accordance with sound business principles, the costs associated with the acquisition, conservation, and transmission of electric power. . . .” Section 7(a)(1), 16 U.S.C. § 839e(a)(1) (emphasis added).

Note also that the rates established by BPA are subject to FERC approval. Section 7(a)(2), 16 U.S.C. § 839e(a)(2). The Ninth Circuit has declared that “One of the fundamental

tenets in FERC jurisprudence is the rule against retroactive ratemaking.” *Public Utilities Comm’n of Cal. v. FERC*, 456 F.3d 1025, 1061 (9th Cir. 2000) citing *Arkansas Louisiana Gas Co. v. Hall*, 453 U.S. 571, 578, 101 S.Ct. 2925, 2930-31, 69 L.Ed.2d 856 (1981).

In addition to the prohibition of retroactive ratemaking, *Bowen* also forbids retroactive rulemaking. 488 U.S. at 208, 109 S.Ct. at 471. In *Bowen*, the Secretary of Health and Human Services promulgated a rule that had a retroactive application. On appeal, the Circuit of Appeals for the District of Columbia held as a general matter that the Administrative Procedures Act, 5 U.S.C. §§ 551, 553 *et seq.*, forbids retroactive ratemaking. *Georgetown University Hospital v. Bowen*, 821 F.2d 750, 757 (D.C. Cir. 1987) (the APA is clear and “equitable considerations are irrelevant to the determination of whether the Secretary’s rule may be applied retroactively”). The Supreme Court affirmed. *Bowen*, 488 U.S. at 208, 109 S.Ct. at 471. The Supreme Court held that “a statutory grant of legislative rulemaking authority will not, as a general matter, be understood to encompass the power to promulgate retroactive rules unless that power is conveyed by Congress in express terms.” *Bowen*, 488 U.S. at 208, 109 S.Ct. at 472. “Even where some substantial justification for retroactive rulemaking is presented, courts should be reluctant to find such authority absent an express statutory grant.” *Id.* at 209, 109 S.Ct. at 472. BPA has no authority empowering it to provide reparation, refunds or any similar retroactive remedy.

D. The Prevailing Parties in PGE and Golden Northwest Failed to Exercise Measures that would have Protected Their Interests

Even though BPA has no power to grant a retroactive remedy³, the prevailing parties in *PGE* and *Golden Northwest* could have preserved the fruits of their appeal by obtaining a stay

³ As noted previously, the Administrator must issue refunds if the final FERC-approved WP-07 rates are less than the interim WP-07 rates. 18 C.F.R. § 300.21(g).

of BPA's WP-02 Order from BPA or the Court. Judicial review of final BPA actions under the APA expressly provides for such a procedure. 5 U.S.C. § 705 (an agency "may postpone the effective date of action taken by it, pending judicial review.").⁴

Likewise, Rule 18 of the Federal Rules of Appellate Practice provides for a stay pending appellate review. Under Rule 18, a petitioner must ordinarily first move BPA for a stay pending review of its decision or final order. FRAP 18(a)(1). In addition, this rule provides that a motion for stay may be made to the Ninth Circuit or one of its judges. FRAP 18(a)(2). As indicated in Attachment 1 to WP-07-E-ID-1, no parties to the underlying appeal sought a stay from BPA, FERC or the Ninth Circuit.

Because BPA's WP-02 rates were not stayed, they remain lawful and valid through the judicial review process consistent with "the well-established rule that an appeal will not affect the validity of a judgment or order during the pendency of an appeal, absent a stay or supersedeas." *Combine Metals Reduction Co. v. Gemmill*, 557 F.2d 179, 190 (9th Cir. 1977). By failing to stay the effects of the WP-02 rate order, the petitioners put themselves at risk of losing the fruits of their appeal. "[Thus,] a party who chooses to appeal but fails to obtain a stay or injunction pending appeal risks losing its ability to realize the benefits of a successful appeal." *Holloway v. United States*, 799 F.2d 1372, 1374 (9th Cir. 1986) (emphasis added and citations omitted), quoting *Matter of Combined Metals Reduction Co.*, 557 F.2d 179, 188 (9th Cir. 1977); *United States v. Peterson*, 19 F.3d 1442, 1444 (9th Cir. 1994) (unpublished disposition). That risk has now materialized.

⁴ Section 705 further provides: "On such conditions as may be required and to the extent necessary to prevent irreparable injury, the reviewing court, including the court to which a case may be taken on appeal from or on application for a certiorari or other writ to a reviewing court, may issue all necessary and appropriate process to postpone the effective date of an agency action or preserve status or rights pending conclusion of the review proceedings." 5 U.S.C. § 705.

E. The Deemer Mechanism is not Authorized by the Northwest Power Act

In *PGE*, the Court explained the operation of the REP mechanism. “Section 5(c) permits IOUs to exchange power they have purchased or generated for lower-cost power generated by BPA.” 501 F.3d 1009, 1015 (emphasis added). Under the program, IOUs sell power to BPA at the IOUs’ average system costs (ASCs) and then purchase and exchange an equivalent amount of BPA power at a lower price. “The REP essentially acts as a cash rebate to the IOUs where the IOUs’ power costs exceed those of BPA.” *Id.* (emphasis added). Section 5(c) of the Northwest Power Act requires that any exchange benefit be passed through to a utility’s residential and small farm customers. *Id.*, 16 U.S.C. § 839c(c)(3).

Although the deemer balances were not mentioned in either of the Court’s opinions, BPA proposes to recover the allegedly outstanding deemer balances. As BPA witnesses explain:

Deemer balances are a remnant of BPA’s implementation of 1981 RPSAs with exchanging utilities. In simple terms, in the event a utility’s ASC was lower than BPA’s PF exchange rate, the utility would not pay cash to BPA but would accumulate a negative balance that had to be paid off before the utility could receive positive REP benefits.

WP-07-E-BPA-52, p. 18, ll. 5-9. When the IOU’s ASC was lower than BPA’s PF rate, the IOU’s “separate account” would be debited but no actual cash payments or power exchange would be made by the IOU to balance the account. The 1981 RSPA states that upon “termination of this agreement, any debit balance [i.e., negative balance] in such account shall not be a cash obligation of the Utility” RPSA § 10, p. 8. This 1981 “phantom” accounting mechanism has real consequences in BPA’s proposal today.

The deemer balances also accrued interest. WP-07-E-BPA-44, p. 196, ll. 15-26. Given the passage of time, the deemer balances have substantially increased as interest has accrued. For example, Idaho Power’s deemer balance allegedly increased from \$52.9 million in

1987 to \$245.36 million as of October 2007 (WP-07-E-ID-1, p. 18, ll. 14-18) based solely on the basis of compound interest. Not all IOUs suffered under compound interest.

There is no statutory authorization for BPA to engage in deemer accounting. As construed by the Ninth Circuit, the Northwest Power Act contemplates that BPA and the IOUs would exchange when an IOU's ASC was above BPA's cost. Section 5(c), 16 U.S.C. § 839c(c). In this fashion, IOUs would receive the benefits of the federal hydropower system. The deemer mechanism is contrary to the plain reading of Section 5(c) of the Northwest Power Act, 16 U.S.C. § 839c(c).

As the Court stated in *PGE*, “whenever BPA engages in a purchase and exchange of power – whether on a yearly basis, under an REP program, or pursuant to a settlement agreement – BPA acts pursuant to its § 5(c) authority, and is thus subject to the Congressionally imposed limitations on that authority as expressed in § 5(c) and § 7(b). 501 F.3d at 1032. In attempting to spread the benefits of cheap federal power as broadly as possible, BPA departed from the REP mechanism contained in the Northwest Power Act. 16 U.S.C. § 839c(c). BPA's de emer accounting mechanism is well outside the REP program that Congress created in the Northwest Power Act.

CONCLUSION

The Administrator's obligation in response to *PGE* and *Golden Northwest* is to implement the Court's holdings, assuming the opinions are not overturned on appeal by the U.S. Supreme Court. The Ninth Circuit invalidated the REP Settlement Agreements, which in turn affects the REP payments to the IOUs and the preferred rates of the COU customers. To remedy the errors in the Residential Exchange Program, BPA should calculate new ASCs for the IOUs using the 2008 ASCM being developed in a separate proceeding.

Given that the WP-02 rates have expired, BPA is legally prohibited from retroactive ratemaking and the fact that the petitioners did not seek a stay pending review, the Administrator's duty is to set new rates prospectively. Because the WP-07 interim rates became effective October 1, 2006 and have not yet been approved as final rates by FERC, these interim rates are subject to refund. Thus, the Administrator's duty and the petitioners' remedy is to establish prospective rates. In addition, BPA acted outside the bounds of its statutory authority in Section 5 of the Northwest Power Act when it created the deemer accounting mechanism. For these reasons, the Lookback mechanism is unnecessary and unlawful and must be discarded.

Respectfully submitted this **3** day of April 2008.

FOR THE IDAHO PUBLIC UTILITIES COMMISSION



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