

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

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

**INITIAL BRIEF OF THE
IDAHO PUBLIC UTILITIES COMMISSION**

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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.* (“PGE”), 501 F.3d 1009 (9th Cir. 2007), *cert. denied*, ___ U.S. ___ (2008), 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.* (“*Golden Northwest*”), 501 F.3d 1037 (9th Cir. 2007), *cert. denied sub nom. Portland General Electric Co. v. Bonneville Power Admin.*, ___ U.S. ___ (2008), 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 (“the Tribes”) 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). On October 5, 2007, the Court denied petitions seeking rehearing and *en banc* on the two opinions.

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, p. 5. Settlement negotiations were unsuccessful and BPA subsequently issued its Federal Register Notice reopening 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 opinions¹ 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, l. 14.

ARGUMENT

BPA’S LOOKBACK MECHANISM IS UNLAWFUL RETROACTIVE RATEMAKING

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 rates expired September 30, 2006. 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 interim rates currently remain in effect pending completion of this supplement proceeding and final FERC approval. On March 4, 2008, BPA

¹ 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).

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 “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 reopened 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 472.²

“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). In particular, IOU customers are not a fungible mass where future customers may be substituted for

² 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 Court 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 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.” *Id.* 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.

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). Even the BPA witness panels recognize that “residential customers of the IOUs are those who will ultimately bear the entire brunt of the application of the Lookback Amounts to reduce future REP benefits paid.” WP-07-E-BPA-76-CC1, p. 96, ll. 7-9.

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).

The rates established by BPA are also 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); *see also* *Consolidated Edison Co. of New York, Inc. v. FERC*, 347 F.3d 964, 966 (D.C. Cir. 2003)(Agreeing with FERC’s assertion that it “lacked the authority under [section 205 of the] the Federal Power Act to revise rates retroactively.”).

In *Consolidated Edison*, the D.C. Circuit Court recognized certain exceptions to the general rule against allowing utilities a retroactive recovery. *Id.* at 969. According to the Circuit Court, the bar against retroactive ratemaking can be satisfied “when parties have notice that a

rate is tentative and may be later adjusted with retroactive effect, or where they have agreed to make a rate effective retroactively.” *Id.*³

The exceptions outlined by the Circuit Court are not applicable to this rate proceeding. As explained above, the FY 2002-2006 rates that BPA seeks to reconstruct in the instant case are not interim, nor are they tentative. *See supra* p. 4. To the contrary, the FY 2002-2006 rates received full FERC approval and expired prior to the Ninth Circuit decisions that precipitated the instant proceeding. *See* WP-07-TE, Vol. 1, p. 35-36, ll. 18-5, 1.

BPA’s proposal to undergo a wholesale reconstruction of previously approved rates stands in stark contrast with FERC’s recognized authority to order refunds for egregious or fraudulent violations of the Federal Power Act. *See California ex rel. Lockyer v. FERC*, 383 F.3d 1006, 1018 (9th Cir. 2004). BPA’s proposal is more analogous to the fact pattern presented to the D.C. Circuit Court in *Columbia Gas Transmission Corp. v. FERC*, 895 F.2d 791 (D.C. Cir. 1990). In *Columbia Gas*, a group of pipeline customers petitioned for redress after FERC allowed certain gas pipeline sellers to recoup past costs over a three-year period through a “retroactive mechanism” devised and approved by the Commission and referred to as purchase gas adjustment clauses. *Id.* at 793. The aggrieved pipeline customers’ objections to the retroactive recovery centered mainly upon the un rebutted fact that the customers that would be forced to absorb the newly authorized costs were “not representative of those who, during those three years, had purchased the gas that was subject to the deferred costs.” *Id.*

³ The Court referred to tariffs with an established rate formula as “a practical application of this principle” because such rates would be perpetually subject to changes consistent with the filed rate formula. *Id.* (citing *Pub. Utilities Comm’n v. FERC*, 254 F.3d 250, 254 (D.C.Cir.2001)). To its credit, BPA has not attempted to characterize the so-called “Lookback Amounts” it seeks to recover from IOU customers via this supplemental rate proceeding or the reconstructed PF Exchange Rate for FY 2002-2006 as even remotely related to filed rate tariffs with formulas.

Ultimately, the Circuit Court held that FERC had violated the clear and express language of the Natural Gas Act which mandates that rate changes be made prospectively only. 895 F.2d at 797. The Circuit Court rejected FERC's argument that on a finding of "sufficient cause" it could waive the filed rate doctrine and stated emphatically that "once a rate is in place with ostensibly full legal effect and is not made provisional, it can then be changed only prospectively." *Id.*; see also *Southern California Edison Co. v. FERC*, 805 F.2d 1068, 1070 n.2 (D.C. Cir. 1986) ("Derived from the filed rate doctrine is the rule against retroactive ratemaking . . ."). Finally, any change to the filed rate can be made only if notice was given to the ratepayers that said rates "were provisional only and subject to later revision." *Id.*

Similar to the pipeline customers in *Columbia Gas*, millions of non-representative residential and small farm customers throughout the Pacific Northwest will be, under BPA's proposal, forced to absorb the deferred costs of participating in the Residential Exchange Program (REP). BPA does not dispute this intergenerational inequity. Rather, the Agency clearly supports this inevitable outcome, stating that "reductions of future REP benefits paid [to IOU customers] due to Lookback Amounts is a direct transfer of dollars from one class of customers to another . . ." WP-07-E-76-CC1 at 4.

The rule against retroactive ratemaking arose amid concerns over allowing utilities to "set rates to recover for past losses." James C. Bonbright et al., *Principles of Public Utility Rates*, (2d.Ed. 1988) p. 198. BPA claims that its Lookback Analysis does not occur in the "typical context in which retroactive ratemaking issues arise." WP-07-E-BPA-76-CC1, p. 3. BPA states that it is merely responding to the Ninth Circuit decisions by "re-running its rate models for the specific purpose of determining the Lookback Amounts for the IOUs that will be dealt with on a prospective, and not retrospective, basis." *Id.* These claims fly in the face of

BPA's own admission that this supplemental rate proceeding is essentially an effort to reconstruct the PF Exchange Rate for FY 2002-2006. *See* WP-07-E-BPA-53-CC1, p. 9.

In summary, BPA argues that while the process of calculating the "Lookback Amounts" for each of the IOUs is, by definition, a procedure that is retrospective in nature, this process cannot be defined as retroactive ratemaking simply because the Agency will seek to recover the purported overpayments, or Lookback Amounts, made to the IOUs and disburse those amounts "to the consumer-owned utilities (COUs) through future reductions to the PF Preference rate." WP-07-E-BPA-76-CC1 at 5. This is a distinction with no real difference. In fact, it is hard to imagine any scenario where a ratemaking authority would run afoul of the rule against retroactive ratemaking because recovery for past losses will nearly always be on a going forward basis. If this sort of Carrollian logic is allowed to define the parameters of "retroactive ratemaking" then the term would quickly be robbed of its meaning.

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 remedy⁴, the prevailing parties in *PGE* and *Golden Northwest* could have preserved the fruits of their appeal by obtaining a stay 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.")⁵

⁴ 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).

⁵ 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.

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 WP-07-E-ID-CC1-AT1, 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 remained 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, absence 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.

THE "DEEMER" MECHANISM IS BEYOND THE SCOPE OF THE NPA

A. Introduction and History

Section 5(c) of the Northwest Power Act authorizes BPA to enter into power exchanges with the six regional IOUs for the purpose of providing rate relief to residential and small farm customers of the IOUs. H.R. Report No. 96-976(I) at 60, 1980 U.S.C.C.A.N. 5989. The power exchanges were intended to provide the IOUs with access to lower-cost federal

power. When it enacted Section 5(c), Congress recognized that the exchange mechanism may not result in parity between the retail rates of BPA's preference customers and the retail rates of the IOUs' eligible customers, "but it should equalize the wholesale costs of the electric power with a resulting benefit to investor-owned utilities' customers." *Id.*

The Ninth Circuit has often explained how the residential exchange operates. For example in *PGE*, the Court stated that "Section 5(c) permits IOUs to exchange power they have purchased or generated for lower-cost power generated by BPA." 501 F.3d at 1015 (emphasis added); *Golden Northwest*, 501 F.3d at 1047; *Washington Utilities and Transp. Comm'n v. FERC*, 26 F.3d 935, 936-37 (9th Cir. 1994); *PacifiCorp v. FERC*, 795 F.2d 816, 818-19 (9th Cir. 1986). Under the Section 5(c) Residential Exchange Program (REP), a regional IOU may elect to sell power to BPA at the IOU's average system cost (ASC) and then purchase and exchange an equivalent amount of BPA power at a lower price. 16 U.S.C. § 839c(c)(7). "The REP essentially acts as a cash rebate to the IOUs where the IOUs' power costs exceed those of BPA." *PGE*, 501 F.3d at 1015 (emphasis added).

Each utility's ASC shall be recalculated whenever a utility seeks approval from its state regulatory commission to change retail rates. *Id.*; 18 C.F.R. § 301.1(b)(5); WP-07-E-JP21-1/2/3, Exhibit C § III(B)(2). A separate ASC will be calculated for each exchanging utility in each of its operating jurisdictions. 18 C.F.R. § 301.1(b)(1); WP-07-E-JP21-1/2/3, Exhibit C, § I. Finally, Section 5(c)(3) of the Northwest Power Act requires that utilities pass through any BPA exchange benefits to the utilities' residential and small farm customers. *PGE*, 501 F.3d at 1015; 16 U.S.C. § 839c(c)(3).

1. The 1981 RPSAs. After enactment of the Northwest Power Act, each of six regional IOUs began negotiating with BPA to develop a 20-year "Residential Purchase and Sale

Agreement” (RPSA). The costs of the RPSA exchanges prior to July 1, 1985 were to be recovered by BPA in the rates charged to the direct service industrial (DSI) customers. 16 U.S.C. § 839e(c)(1)(A). At that time, some parties argued that if a utility’s ASC fell below BPA’s PF Exchange Rate, the utility should pay BPA the difference in cash. WP-07-E-BPA-62, p. 7-8, ll. 25-1.

BPA and the IOUs entered into their respective RPSAs in 1981. Under Section 2 of the RPSAs, BPA was obligated to exchange power with the regional utilities when the utilities’ ASCs were higher than the BPA PF rate. WP-07-E-JP21-1/2/3, § 2. However, the RPSAs for Avista, Idaho Power and Northwestern also contained a section addressing instances when a utility’s ASC might be lower than BPA’s PF rate. For these three utilities, Section 10 (“Election to Equalize Rates”) provided that a utility with an ASC lower than the PF rate may elect to have its ASC “deemed equal”⁶ to the PF rate. *Id.*, § 10. Rather than discontinuing the exchange, the utility would accumulate a “negative” deemer balance but not pay “cash” to BPA. WP-07-E-BPA-52, p. 18, ll. 5-9; WP-07-E-ID-1CC, p. 11, ll. 8-17. Thus, the deemer mechanism acted as a short-term balancing account: BPA provided exchange benefits to the three IOUs when the utilities’ ASCs are higher than BPA’s PF rate. But when an IOU’s ASC was lower than the exchange rate, the utilities would accumulate a negative balance owed to BPA. Because the utilities’ ASCs were to be recalculated whenever the utilities retail rates changed, the deemer balancing account would apparently net the frequent exchange credits and debits.⁷ For example,

⁶ The phrase “deemed equal” appears to be the source of the term “deemer.”

⁷ The IPUC recognizes that Avista, BPA, and Idaho Power have all asserted that the deemer balances are in dispute. WP-07-E-BPA-44-CC1, p. 208, ll. 1-4; WP-07-E-BPA-76, p. 68, ll. 21-22. The Idaho PUC encourages the parties to settle their deemer disputes. In the mean time, BPA has used the deemer balances in its calculations of the respective Lookback amounts. Although BPA states that it is not making a final determination regarding the deemer balances, it acknowledges that the deemer balances were used for the ratemaking purposes of the docket. WP-07-E-BPA-76, p. 67, ll. 16-21, 23-25. Consequently, the legality of the deemers and the deemer calculations are at issue in this proceeding.

during 1982-83, Idaho Power made several ASC filings. E.g., *Idaho Power Company*, Docket No. ER82-618-000 et al., 30 F.E.R.C. ¶ 63059 (March 8, 1985).

Section 10 also provided, BPA “shall debit to a separate account the net exchange payment to Bonneville.” WP-07-E-JP21-1/2/3, § 10. This section also states that upon “termination of this agreement, any debit balance in such separate account shall not be a cash obligation of the Utility, but shall be carried forward to apply to any subsequent exchange by the Utility for the Jurisdiction under any new or succeeding agreement.” WP-07-E-JP21-1/2/3, § 10, at p. 8 (emphasis added).

Under BPA’s proposed Lookback mechanism, the purported deemer balances must be repaid before exchanging utilities are eligible to receive future REP benefits. WP-07-E-BPA-44-CC1, p. 195, ll. 25-32. BPA asserts that REP benefits would not be available to the three IOUs with deemer balances (Avista, Idaho Power, and Northwestern) until the deemer balances are satisfied. BPA calculated that as of October 1, 2007, Avista’s deemer balance was \$99.3 million and Idaho Power’s deemer balance was \$245.36 million. WP-07-E-ID-1CC, p. 18; WP-07-E-ID-5, p. 16; WP-07-E-ID-4, p. 28. By way of comparison, Avista received REP benefits of \$6.55 million and Idaho Power received REP benefits of \$42.34 million between FY 1982 and FY 1994. WP-07-E-ID-2, p. 9, ll. 8-11; WP-07-E-ID-2-AT16.

2. The Suspension Agreements. In 1983, BPA initiated a proceeding to revise its original ASC methodology. On October 1, 1984, FERC approved the revised methodology. The revised methodology had the general effect of reducing the average system costs for the IOUs. *PacifiCorp v. FERC*, 795 F.2d at 819. Thereafter, Avista in 1987 and Idaho Power in 1988 entered into “suspension” agreements with BPA that suspended the operation of the their 1981 RPSAs. WP-07-E-ID-2CC, p. 7, ll. 11-14; WP-07-E-ID-2-AT6; WP-07-E-ID-2-AT7. The

utilities' Suspension Agreements are generally identical except that Idaho Power's agreement calls for quarterly compound interest (WP-07-E-ID-2-AT6, p. 4, ¶ 4), while Avista's agreement calls for quarterly simple interest. WP-07-E-ID-2-AT7, p. 4, ¶ 4.

3. Termination of the RPSAs. Both Avista and Idaho Power terminated their 1981 RPSAs in 1993. Avista's termination notice simply stated that Avista gives notice "of its election to terminate its 1981 RPSA effective September 30, 1993. . . ." WP-07-E-ID-2CC, p. 9, ll. 18-19 *citing* WP-07-E-ID-2-AT8. In comparison, Idaho Power's termination notice was effective September 30, 1993, and recognized continuation of compounded quarterly interest. WP-07-E-ID-2-AT9.

B. The Deemer Mechanism is not Authorized by the NPA

There is no statutory authorization for BPA to utilize the deemer mechanism or 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 lower-cost benefits of the federal hydropower system. There is nothing in the Northwest Power Act or its legislative history that suggests that the exchange benefits should flow in the opposite direction – from the three IOUs to BPA. Indeed, Section 5(c) was intended to provide residential and small farm customers "a share in the economic benefits of the lower-cost federal system," i.e., lower rates. H.R. Report No. 96-976(I) at 27, 60, 1980 U.S.C.C.A.N. at 5993, 6026. Instead of conferring a benefit, the operation of the deemer mechanism turns Section 5 on its head. As the facts in this case bear out, the "phantom" accounting of accruing negative deemer balances simply because the IOUs' ASC was subsequently lower than BPA's PF rate is extremely detrimental to IOU ratepayers, especially to the more than 400,000 eligible customers of Idaho

Power. Under BPA's proposal to collect Idaho Power's accumulated deemer balance of \$245 million, Idaho Power's current and future customers in Idaho and Oregon would not be eligible to receive REP benefits for the next 20 years. In fact, Idaho Power's deemer account has merely accrued interest since FY 1985. The deemer mechanism is simply contrary to the plain reading and intent 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. “[W]henver BPA exchanges power with a Pacific Northwest utility, it [must] act pursuant to its § 5(c) power[.]” *Id.* at 1028. BPA's deemer accounting mechanism is well outside the REP program that Congress created in the Northwest Power Act. 16 U.S.C. § 839c(c).

C. Collection of the Deemers is Barred by Regulation

Although BPA recognizes that the deemer balances are not cash obligations of the utilities, it asserts that “BPA may contractually set off [the deemer balances] against future REP benefits.” WP-07-E-BPA-76, p. 72, ll. 18-20 (emphasis added). Despite BPA's assertion to the contrary, the Department of Energy (DOE) has promulgated a regulation that prohibits BPA from offsetting the deemer balances against future REP payments. In pertinent part, the DOE regulation states:

Unless otherwise provided by law, administrative offset of payments under the authority of 31 U.S.C. 3716 to collect a debt may not be conducted more than 10 years after the Government's right to collect the debt first accrued, unless fact materials to the Government's right to collect the debt were not known and could not reasonably have been known by the official or officials of the Government who were charged with the responsibility to discover and collect such debts.

10 C.F.R. § 1015.203(a)(4) (emphasis added). In addition, 31 U.S.C. § 3716(e)(1) prohibits the Government from pursuing an administrative offset for claims that have been outstanding for more than 10 years. Section 3701 defines a “claim” as “any amount of funds . . . owed to the United States” including over-payments (e.g., REP benefits). 31 U.S.C. § 3701(b)(1)(C).

Avista and Idaho Power both suspended their RPSAs with BPA in 1987 and 1988, respectively. WP-07-E-ID-2, p. 7, ll. 11-14; WP-07-E-ID-AT7; WP-07-E-ID-AT6. Avista and Idaho Power also terminated their 1981 RPSAs in 1993. WP-07-E-ID-1CC, p. 19, ll. 19-20. Since that time, BPA has had ample opportunity to assert its right to offset the alleged deemer balances against the residential exchange benefits distributed to the three IOUs. Given BPA’s failure to pursue its claim to recover the deemer balances, the DOE regulation prohibits BPA from collecting the deemer balances now. 10 C.F.R. § 1015.203(a)(4).

BPA’S CALCULATIONS OF THE DEEMER BALANCES ARE ARBITRARY AND NOT SUPPORTED BY THE TOTALITY OF THE EVIDENCE

A. BPA’s Use of Different Methods to Calculate Deemer Interest is Arbitrary

Although the 1981 RPSA contracts for Avista, Idaho Power and Northwestern are identical, BPA used different methods of calculating the interest on the deemer balances. For Idaho Power and Northwestern, BPA used compounded interest to calculate the respective deemer balances, but for Avista it used simple interest to calculate Avista’s deemer balance. WP-07-E-BPA-44-CC1, p. 196, ll. 12-26; WP-07-TE, Vol. 1, p. 90 at ll. 1-2. Idaho PUC witness Westerfield testified that BPA’s use of simple versus compound interest has a significant effect on the calculations of the deemer balances. For example, Avista’s purported deemer balance grew 2.5 times from the accumulation of only interest between January 1987 and October 1, 2007 (to \$99.3 million). WP-07-E-ID-1CC, p. 18, ll. 7-12; WP-07-E-ID-5. In comparison, BPA’s use of compound interest increased Idaho Power’s purported deemer balance 4.2 times

(interest only) between January 1987 and October 1, 2007 (\$245.36 million). WP-07-E-ID-1CC, p. 18, ll. 13-20; WP-07-E-ID-4.

When asked to explain why Avista's deemer balance was calculated using simple interest but Idaho Power's deemer balance was calculated using compound interest, the BPA panel offered no explanation other than the wording of the utilities' respective Suspension Agreements (WP-07-E-ID-2-AT6 and AT7). WP-07-TE, Vol. 1, p. 90-91, ll. 23-6. Avista's principal deemer balance has not changed since January 1987 and the growing balance merely represents the accrual of simple quarterly interest at the prime rate. WP-07-E-ID-2, p. 8, ll. 13-14; WP-07-E-ID-5. On the other hand, BPA's Excel spreadsheet for the calculation of Idaho Power's deemer balance (WP-07-E-ID-4) reflects that using the compound method, interest is added to the principal and this "new" subtotal or principal balance is then subject to quarterly interest at the prime rate. WP-07-E-ID-2, p. 8 at ll. 7-12; WP-07-E-ID-4.

The use of two different interest rates (i.e., simple versus compound) for similarly situated utilities is arbitrary and discriminatory. There is no evidence in the record and BPA has not offered any logical explanation why BPA uses simple interest to calculate Avista's deemer balance, but used compound interest to calculate Idaho Power's deemer balance. The 1981 RPSAs of the two companies are identical as are the subsequent Suspension Agreements but for the issue of simple versus compound interest. The circumstances between the two companies are indistinguishable yet BPA has intentionally treated them differently in calculating their deemer balances. The use of difference interest methodologies to calculate the deemer balances in this instance is clearly unreasonable and arbitrary. 5 U.S.C. § 706(2)(a).

Applying compound interest to Idaho Power's deemer balance also has a punitive effect. By adding the purported deemer balances to the Lookback amount, more than 400,000

Idaho Power residential and small farm customers will be deprived of any REP benefits for more than 20 years into the future. WP-07-E-ID-1CC, p. 12, ll. 1-15; WP-07-TE, Vol. 1, p. 95-96, ll. 23-9. Even BPA's Lookback Study calculates that Idaho Power would not amortize its Lookback amount (\$96.56 million) and its deemer balance (\$245.36 million) by the year 2028. WP-07-E-BPA-44-CC1, p. 207, ll. 25-27; WP-07-E-BPA-44-CC1, p. 201, Table 15.4. Is it inequitable to withhold REP benefits from present and future customers because past customers received the benefit of BPA's inappropriate rates.

***B. The Totality of the Evidence Does Not Support
BPA's Calculations of the Deemer Balances***

1. The 18-Month Gap. In May 1985, FERC approved a Settlement Agreement among BPA, Idaho Power and each DSI customer. As part of the Settlement Agreement, BPA paid Idaho Power \$7.5 million and credited its deemer account a total of \$6.7 million (for its jurisdictions in Idaho, Oregon, and Nevada). WP-07-E-ID-2CC, p. 4, ll. 10-16; WP-07-E-ID-2-AT4, p. 6-7. Following FERC's approval of the 1985 Settlement Agreement, Idaho Power asked BPA in a letter dated June 18, 1985 to confirm Idaho Power's deemer balance as of May 31, 1985. WP-07-E-ID-2-AT5. In the letter, BPA confirmed by counter-signature that Idaho Power's total deemer balance (for its Idaho, Oregon, and Nevada jurisdictions) totaled \$8,068,020.50 as of May 31, 1985. *Id.* BPA's witness panel agreed that this amount was the correct deemer balance for Idaho Power as of May 31, 1985. WP-07-TE, Vol. 1, p.115-16, ll. 21-3.

In the BPA Excel spreadsheets used to calculate Idaho Power's purported deemer balances (WP-07-E-ID-4), BPA used a beginning balance for Idaho Power's three jurisdictions totaling approximately \$58,154,151 as of January 1987. WP-07-E-ID-2, p. 5, ll. 12-15. On cross-examination, BPA witness panels could not explain how Idaho Power's deemer balance

could increase from approximately \$8 million to more than \$50 million in the 18 months between May 31, 1985 and January 1987. WP-07-TE, Vol. 1, p. 137, l. 7. Moreover, Idaho Power received no REP benefits after FY 1985. WP-07-E-ID-2-AT16. The BPA panels said that they had no information on the deemer balances prior to 1987 and simply relied on the deemer balances identified in the Suspension Agreements. WP-07-TE, Vol. 1, p. 93-94, ll. 23-12.

2. Nevada Benefits. In addition, it was unrefuted that Idaho Power sold its Nevada service area to an Idaho electric co-operative in 2001. WP-07-E-ID-1CC, p. 13, ll. 17-21; WP-07-E-ID-1-AT2. Consequently, it is inappropriate to collect the Nevada deemer balance of \$2.9 million from the remaining Idaho Power customers in Idaho and Oregon. WP-07-E-ID-4, p. 28.

3. Treasury v. Prime Rate. The 1981 RPSAs for Avista, Idaho Power and Northwestern state that the “net balance in [the deemer] account shall accumulate interest at the rate specified in Section IV.E. of Exhibit C.” WP-07-E-JP21-1/2/3, p. 7. That portion of Exhibit C provides in pertinent part

If Bonneville determines that the ASC computed by the Utility in Appendix 1 is excessive or inadequate, the injured party shall recover the excess or deficiency with interest which shall be computed from time to time on the outstanding balance at the rate or rates of interest charged to Bonneville by the U.S. Treasury during the period unless another form of refund is ordered by the Joint State Board, the FERC, or a reviewing court.

WP-07-E-JP21-1/2/3, Exhibit C, p. 5 of 7 (emphasis added). Thus, the 1981 RPSAs for these three utilities set the interest rate for the deemer mechanism at the “Treasury rate.”

Although the 1981 RPSAs provided that interest on the deemer balances would accrue at the Treasury rate, BPA utilized the prime rate to calculate the quarterly interest on the deemer balances before the effective date of Idaho Power’s Suspension Agreement, August 1, 1988. Compare WP-07-E-ID-2-AT6 with WP-07-E-ID-4, p. 1, 10, 19. The same error applies

to the calculation of Avista's deemer balance. *Compare* WP-07-E-ID-2-AT7 with WP-07-E-ID-5, p. 1, 8. On cross-examination, the BPA panel could not explain when the Treasury rate changed to the prime rate or the reasons for such a change. WP-07-TE, Vol. 1, p. 135-36, ll. 17-24. In the Excel spreadsheets used to calculate the deemer balances for Avista and Idaho Power, BPA utilized the prime rate instead of the Treasury rate before the prime rate was specified in the two utilities' Suspension Agreements.

Given the unexplained increase in Idaho Power's deemer balance for 18 months, the arbitrary use of two interest methodologies, the inclusion of the Nevada deemers for Idaho Power and the use of the erroneous interest rate (Treasury v. prime), the totality of the evidence does not provide adequate support for BPA's deemer calculations. As outlined above there is substantial evidence that BPA's deemer balances are incorrect. 5 U.S.C. § 706(2)(E); *Robert F. Kennedy Medical Center v. Leavitt*, ___ F.3d ___, 2008 WL 2080238 (9th Cir. 2008).

**BPA'S FAILURE TO RECORD THE DEEMER BALANCES IN ITS
FINANCIAL BOOKS VIOLATES GENERALLY ACCEPTED
ACCOUNTING AND RATEMAKING PRINCIPLES**

BPA acknowledges that it follows FERC's Uniform System of Accounts in maintaining its financial books and records. WP-07-TE, Vol. 1, p. 98, ll. 5-7. BPA also follows the U.S. Department of Energy's (DOE's) accounting order RA 6120.2, entitled "Power Marketing Administration Financial Reporting," which states: "Power system financial statements will be prepared in accordance with generally accepted accounting principles." WP-07-E-ID-CC1, p. 16, ll. 7-24; *Order Confirming and Approving Rates*, Docket No. EF03-2011-000, 107 FERC ¶ 61138 n.2 (May 10, 2004).

However, by BPA's own admission, the deemers have never been recorded in BPA's books and accounts. WP-07-E-ID-1CC-AT3(BPA's response to Data Request PU-BPA-5).

BPA's failure to record the deemer balances in its financial records is contrary to generally accepted accounting principles, as well as ratemaking principles. Neither generally accepted accounting principles, nor FERC's Uniform System of Accounts, nor DOE's accounting order RA 6120.2 sanction "off the books" accounting for transactions. WP-07-E-ID-1CC, p. 17, ll. 13-15. Therefore, BPA cannot now propose to include these "off the books" amounts in the Lookback Analysis and, thus, in rates in violation of accounting and ratemaking principles.

Absent a legitimate audit trail in BPA's records, the deemer balances cannot be substantiated or verified. Instead, BPA maintains the calculation of the deemer balances for Avista and Idaho Power in Excel spreadsheets that are unaudited. WP-07-E-ID-4; WP-07-E-ID-5. This type of documentation cannot substitute for a durable accounting record.

BPA has had every opportunity over a long period of time to record the deemer balances in its books and records, but has chosen not to do so. BPA's rationale now for not recording the deemers is that, as things have turned out, the deemer balances were not collected. (WP-07-TE, Vol. 1, p. 99-100, ll. 21-18). This rationalization using hindsight to explain BPA's lack of adherence to generally accepted accounting principles is absurd.

Finally, Section 10 of the 1981 RPSAs specifies that BPA "shall debit to a separate account the net exchange payment to Bonneville." WP-07-E-JP21-1/2/3, § 10. The plain meaning of "separate account" is an account contained in BPA's financial books and records – not an account kept somewhere else.

CONCLUSION

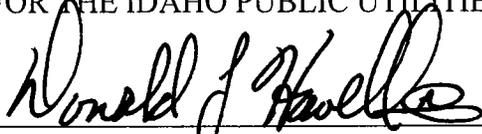
The Administrator's obligation in response to *PGE* and *Golden Northwest* is to implement the Court's holdings. The Ninth Circuit invalidated the REP Settlement Agreements, which in turn affects the REP payments to the IOUs and the preferred rates of the COU

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 prohibited from retroactive ratemaking. This position is further supported by the fact that the petitioners in the two court appeals did not seek a stay pending review. Thus, 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. The Administrator's duty and the petitioners' remedy is to establish prospective rates with the WP-07 rate being subject to refund back to October 1, 2006. Finally, BPA acted outside the bounds of its statutory authority in Section 5 of the Northwest Power Act when it created the deemer accounting mechanism. Moreover, BPA has made several material errors in calculation the deemer balances. For these reasons, the Lookback and deemer mechanisms are unnecessary and unlawful and must be discarded.

Respectfully submitted this 11th day of June 2008.

FOR THE IDAHO PUBLIC UTILITIES COMMISSION



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