

THE LONGVIEW STORY

This is the true story of how the Bonneville Power Administration (“BPA”) squandered millions of dollars helping a company with no assets to purchase an old, operating aluminum smelter in Longview, Washington State.



BPA tried to cover up its mistake by conducting a sham audit of the transaction and giving misleading answers to members of Congress who asked about what happened to the money.

BPA staff say the story is old -- the key events took

place six years ago -- and that BPA was the innocent victim in the arrangement when it signed the contract to finance the purchase of the Longview aluminum smelter.

But court records and other documents tell a different story, a tale of how BPA bent over backwards to please a group of Illinois businessmen. BPA failed to use normal business due diligence: it did not even request to see a bank statement before it wrote a series of checks totaling \$226 million to a company called Longview Aluminum, LLC.

The company then used BPA funds for a number of questionable expenditures, such as life insurance policies for officers and directors, while it was laying off 925 workers at the smelter. Although BPA knew of these actions, it did nothing.

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We investigate BPA's \$226-million contract with Longview Aluminum LLC.

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Why is the Longview story relevant now?

The Longview story is important for three reasons:

First, BPA management ought to be held responsible for its actions. Many workers at the smelter lost a portion of their retirement and all of their medical benefits because of BPA's decisions. Yet BPA has never admitted it did anything wrong. What does that suggest about BPA's concern for avoiding the same mistake again?

Second, Congress and the Secretary of Energy ought to ask probing questions of BPA. Records show BPA signed the \$226-million contract in 2001 without even informing the U.S. Department of Energy. How much money does BPA have to spend before it triggers a review by the Department?

Third, BPA wants to sign new, long-term power sales contracts with utility customers and aluminum companies in 2008. The Longview story ought to trigger a debate before those utilities and companies sign up with BPA as their power supplier.

When money goes out BPA's door, as it did in the Longview transaction, BPA recovers those expenses from its utility customers. The utilities, in turn, pass on BPA's costs to 12.5 million people in the region. If you live in Washington, Oregon, Idaho or western Montana, you paid for BPA's mistake in the Longview transaction, and you will be forced to pay for BPA's next mistake.

It may be difficult for some readers to believe the BPA transaction with Longview happened, but the documents verify the accuracy of the statements made in this article: read on, and make up your own mind. The materials used for this article are all in the public domain. Notes at the end of the article contain the citations.

The Setting

Our story begins in Longview, a small industrial town lying on the edge of the Columbia River in Cowlitz County, southwest Washington State.

It was there in 1941 that the Reynolds Metals Company built an aluminum smelter, only months before the United States entered the Second World War. During the war, BPA sold power to

the Longview smelter and others that made aluminum for military uses. After the war, BPA continued to serve the Longview smelter and energy-intensive industries known as the Direct Service Industries ("DSIs"). In 1968, Reynolds expanded the Longview smelter by building a north plant adjacent to the World War II-vintage south plant. BPA supplied power for the expanded facility, too.

You paid for BPA's mistake in the Longview transaction in your power bill.

Over the years, Reynolds had established itself as a prosperous global company with plants in the United States, Europe and elsewhere. The Longview smelter, located on 600 acres, employed 925 people and produced high-purity aluminum ingots.

Reynolds, however, was not the biggest aluminum company in the world. That distinction belonged to the Aluminum Company of America ("Alcoa"), founded in 1888 and located in Pittsburgh. It, too, owned smelters in Washington State and was a long-standing BPA customer.

In 1999, Alcoa announced it would acquire Reynolds. But the merger needed approval from the European Union (where both Alcoa and Reynolds owned plants) and from the U.S. Department of Justice.



The Longview smelter in the 1940s.

The Entrepreneurs

In Chicago, the proposed merger of Alcoa and Reynolds attracted the attention of a group of businessmen who objected to the marriage of the nation's two largest aluminum companies. Leading this effort was Michael W. Lynch, one of the founders of Michigan Avenue Partners, a privately-held investment firm created in 1992.

Michigan Avenue Partners acquired distressed real estate properties and manufacturing firms in the Midwest. It controlled as many as two dozen companies, which loaned money to each other and engaged in affiliate transactions.

One of the affiliates, McCook Metals LLC ("McCook"), owned a plant in McCook, Illinois, west of Chicago. The McCook plant manufactured an aluminum-lithium alloy for military and space applications, and it competed with Alcoa for sales to the federal government. McCook depended on the Reynolds smelter in Longview for its supply of high-grade aluminum, a special product known as P0404. McCook officials feared that Alcoa, as owner of the Longview plant once the merger was complete, would raise prices and damage McCook's competitive position.¹

To protect its interests, McCook asked the European Union to require Alcoa to sell its entire interest in the Longview smelter. In May 2000, the EU handed McCook a partial victory: it ordered Alcoa to divest itself of 25% of the Longview smelter. The U.S. Justice Department, however, approved the merger without imposing the same condition.

McCook immediately filed an antitrust lawsuit against Alcoa in federal district court, seeking to compel complete divestiture of the

Longview smelter.² Three months later, in August 2000, the parties reached a tentative agreement. Alcoa would sell the entire smelter to McCook for \$155 million.³ McCook, in turn, would dismiss its antitrust lawsuit.

By this point, however, McCook was in financial difficulty. Its chief creditor, the General Electric Capital Corporation ("GECC"), had placed McCook on its internal "watch list" of financially-troubled companies to whom it had lent money.⁴

In its press releases, McCook portrayed itself as a small, courageous company fighting Alcoa's corporate dominance. The truth was less compelling. McCook was not able to buy the Longview smelter without help, and it had tried unsuccessfully to obtain financing from conventional sources.⁵

Finding no other avenue for help, McCook turned to BPA, a federal power marketing agency in Portland, Oregon. BPA's core mission is to sell and deliver power from federal dams and other sources to the region's electric utilities. BPA has the legal authority to sell power to aluminum smelters, but it has no responsibility to keep

Federated Aluminum Council, an umbrella of unions at the smelter.

Nonetheless, BPA was willing to sign new five-year power sales contracts with smelter owners that wanted to do so. McCook told BPA that five years was too short a period. McCook asked BPA for special treatment: it wanted a cheap power supply from BPA for 10 years for the Longview smelter.⁷

To bolster its case, McCook told BPA it had developed a new alloy that would allow airplane manufacturers to make airplanes without rivets.⁸ McCook, they said, would convert the aging Longview smelter into a modern, efficient plant.

On its face, McCook's assertions should have raised eyebrows. Airplanes with no rivets? BPA staff, however, appeared to have accepted the company's word without ever asking for documentation. An internal e-mail distributed within the agency said:

"McCook of Illinois has developed a process for producing aluminum alloy that can be welded. This product has a potentially substantial application in aircraft manufacturing as it would do a way [sic]

them in business if they cannot make it on their own. But that did not stop BPA from coming to McCook's assistance. BPA's behavior was particularly curious because McCook was not a BPA customer and had no assets in the Pacific Northwest.

Airplanes With No Rivets?

In 2000, the aluminum industry in the Pacific Northwest had its own problems. The price of aluminum had dropped. It was not clear how many smelters, particularly old facilities like Longview, could survive in those uncertain economic conditions. Alcoa had shut down an aging smelter in Troutdale, Oregon, which it acquired from Reynolds as part of the merger.⁶

Workers at the Longview smelter feared Alcoa would do the same thing with their facility. Half the plant (the south part) dated back to World War II. The newer half (the north part) had environmental compliance problems and relied on a technology that Alcoa did not seem to favor. "We thought of ourselves as the ugly little stepchild in the Alcoa family," recalled Wes Wheeler, a 25-year veteran employee and head of the Longview



with the need to use rivets in airplane construction. McCook would like to locate its production facility for this new alloy in the Northwest closer to major aircraft construction centers in Washington state and California."⁹

McCook told BPA it had developed a new aluminum alloy that would allow for the manufacture of airplanes with no rivets.

BPA wanted the owners of the Longview smelter to modernize it and make it more efficient.

Because of the potential economic benefits to the region, BPA said:

"McCook and BPA are discussing a conceptual approach... that would help McCook secure financial backing so it could purchase Alcoa's Longview aluminum plant, modernize it and keep it operating competitively in the world market."¹⁰



McCook wanted BPA to act promptly, and it went to Congress for political support. The company asked the four U.S. senators from Washington and Oregon to pressure BPA to sell cheap power to the Longview smelter for 10 years. McCook promised it would build its own power plant to become sufficient by 2011.

On October 20, 2000, Sen. Murray (D-WA), Gorton (R-WA), Wyden (D-OR) and Smith (R-OR) wrote BPA, expressing tacit support for McCook's proposal. "McCook will need some creative help from Bonneville in the near term," the letter said. "We specifically want to avoid micro-managing BPA. However, if the [McCook] proposal meets the advantages above without impacting Northwest ratepayers, we urge you to support and work to implement it."¹¹

BPA, however, declined to sign a special 10-year power sales contract for the Longview smelter.

Instead, BPA signed five-year contracts with the region's smelters, including Alcoa, still owner of the Longview plant, pending final contract negotiations with McCook.¹²

Alcoa's contract with BPA was for only half of the historic amount of power consumed at the smelter, a decision that apparently reflected Alcoa's interest in keeping only the newer north plant in operation.

BPA's New Administrator

That was where matters stood when BPA Administrator Judi Johansen announced on November 9, 2000, that she had accepted a job as vice president of PacifiCorp, an investor-owned utility in Portland.

Stephen Wright succeeded her as Administrator.¹³ Wright was a career BPA employee who had held various positions at the agency, the longest of which was as the head of its Washington, D.C. office.

Wright assumed his duties in the midst of a West Coast energy crisis with unprecedented high prices and volatility. In addition, one of the worst droughts on record had hit the Pacific Northwest. The drought reduced the amount of power that BPA could sell from federal dams and put even more financial pressure on BPA to curtail power use.¹⁴ Put

simply, BPA had too many customers and not enough power.¹⁵

In December 2000, only two months after BPA signed the new contracts with Alcoa and other smelters, BPA proposed a solution. BPA said it would "buy back" its obligations to sell power to the companies.¹⁶



The amount of money -- in theory -- that BPA paid the smelters to curtail power usage would be *less* than what BPA would have to pay for purchased power on the open market. By curtailing the smelters, BPA would cut its losses.¹⁷

One of the smelters that BPA wanted to shut down was Longview, even though there were signs, at least to union officials, that Alcoa would soon close half the smelter (the older south plant) and perhaps the entire facility, no matter what happened.

BPA, however, was uninterested in these

distinctions. BPA staff seemed to be in a full-blown panic about reducing power consumption, no matter what it cost.

McCook now had the opening it needed. McCook's representatives let BPA know they were interested in a "buy back" (curtailment) arrangement *if* BPA's cash payments were high enough so McCook could buy the Longview smelter from Alcoa. McCook officials believed they could make the entire Longview smelter into a money-making facility even in those difficult economic times. But McCook needed BPA's money to do so.

McCook's Negotiating Team

For help, McCook had lined up a strong negotiating team, including former BPA Administrator Randy Hardy (a consultant in private practice), as well as lawyers and lobbyists in Chicago and Washington, D.C.¹⁸ McCook also hired former BPA general counsel Harvard Spigal, a partner with Preston Gates & Ellis in Portland.

BPA agreed in principle with McCook's curtailment proposal. BPA promised to pay cash to McCook so it could buy the smelter from

Alcoa. McCook, in turn, promised to shut down the smelter immediately, thus relieving BPA of having to buy power for the facility.

McCook then created a new corporation to buy the Longview smelter. In November 2000, it formed Longview Aluminum, LLC ("Longview Aluminum").¹⁹ Michael W. Lynch -- board chairman, CEO and largest shareholder of McCook -- served in the same capacity with Longview Aluminum. Longview Aluminum, however, existed chiefly on paper. Unlike McCook, which had real assets (though it was in financial trouble), Longview Aluminum was a shell. It had no assets or revenue stream, except for what BPA promised to provide.²⁰

Longview Aluminum LLC had no revenue, except what BPA promised to provide. BPA was its "bank."

With BPA's assurances of help, Longview Aluminum obtained temporary

financing in December 2000 from a private equity fund and other lenders to buy the smelter from Alcoa. The price: \$140 million. The amount was less than the tentative price of \$155 million agreed to only a few months earlier but was still a huge sum for a company whose chief asset was BPA's pledge of largesse.²¹

An "Innovative Agreement"

On February 27, 2001, BPA and Longview Aluminum formally signed a \$226-million "curtailment agreement." The agreement obligated Longview Aluminum to stop buying BPA power immediately and for BPA to pay money to the company in installments during a 16-month period.

On March 1, 2001, Administrator Wright held a press conference in Portland with Longview Aluminum board chairman and CEO Michael W. Lynch, union officials and others to explain the "innovative agreement."²²

Wright told reporters that BPA's \$226-million agreement was good for the region. Not having to supply power to the smelter "is a tremendous benefit to Northwest ratepayers

because we will not have to go out and buy power on the open market," Wright said.²³

In exchange for the \$226 million, Wright said McCook -- there was no mention of Longview Aluminum -- would do the following things:

- Pay workers when the smelter was shut down;
- Upgrade the entire plant during the shut-down period to create a "state of the art" efficient facility;
- Buy BPA power again starting in 2002, but for only half the smelter; and
- Build its own power plant to make the smelter completely self-sufficient by 2006.



The 2006 date was five years earlier than McCook proposed when it first approached BPA. But CEO Lynch seemed unfazed by the schedule, which would have been ambitious even for an experienced power plant builder. Lynch said his firm would work with

Enron to build a large gas-fired power plant at the Longview site.²⁴

According to Lynch and BPA, McCook planned to retrofit the entire smelter and bring it back into operation, even though BPA was obligated to sell it power in 2002 for only half the historic amount. Neither BPA nor Lynch explained where Longview Aluminum would get the remaining power to keep the entire facility in operation.

BPA omitted key facts at its press conference.

But there were other omissions in BPA's press releases and public statements. BPA did not refer to Longview Aluminum, the newly-created company that would own the smelter. By calling the company "McCook" in its press release, BPA relieved itself of having to explain how Longview Aluminum, whose only asset was BPA money, could refurbish an aging smelter and build a new power plant. Those items were hugely expensive and would cost hundreds of millions of dollars.

Nor did BPA disclose that its payments to Longview Aluminum were three times more per megawatt hour ("MWh") than what BPA paid other smelters to curtail power usage. Other smelters received about \$20 per MWh from BPA to curtail their power demands for a year or two. BPA paid \$60 per MWh to Longview Aluminum. The difference -- equivalent to \$150 million -- was what the company needed to buy the Longview smelter from Alcoa and repay the temporary loans it had assumed months earlier.²⁵

Where The Money Was Supposed To Go

After repaying the lenders, and buying the smelter from Alcoa, and paying the workers, Longview Aluminum had about \$29 million left. That was the "pot of money" that Longview Aluminum could tap to retrofit the smelter and build a new power plant. But the BPA contract did not establish deadlines for the company to spend this money.

Clearly, the \$29 million would not go far. Longview Aluminum would have to rely on McCook or other affiliate companies in the McCook corporate empire for help in retrofitting the

smelter and building a power plant.²⁶

Under its BPA agreement, Longview Aluminum had to tell BPA each time it withdrew any of the \$29 million, which the company placed in a “corporate proceeds account.”²⁷ BPA had the right to audit the withdrawals to make sure Longview Aluminum spent BPA’s money for “qualified expenditures,” such as smelter upgrades and expenses for the new power plant.²⁸ If BPA, as a result of the audit, determined the withdrawals were not used for qualified expenditures, then BPA could order Longview Aluminum to put back the money in the account within 30 days.²⁹



At the Longview smelter, the terms of the BPA curtailment agreement were greeted with relief: the workers would be paid during the 16-month shut-down. “We are going to

be a long-term player in the Pacific Northwest,” Michael W. Lynch told the *Longview Daily News*, which described the 40-year-old executive as a colorful entrepreneur whose “cufflinks match the colors in his tie, and his tie matches the pinstripe suit.”³⁰

The Unraveling

Only a month after the BPA press conference, the arrangement began to unravel. On March 2001, Longview Aluminum announced it would terminate 40 salaried employees.³¹

Then, in April, McCook, which had originally approached BPA for help to buy the Alcoa smelter, filed for Chapter 11 bankruptcy protection.³²

More trouble at McCook followed soon. In September, McCook chairman and CEO Lynch resigned and began taking his salary from Longview Aluminum.³³ But his replacement at McCook immediately ousted four remaining directors amid allegations of fraud, dishonesty, incompetence and mismanagement.³⁴ Weeks later, McCook’s largest creditor, GECC, asked a bankruptcy court to appoint a trustee because

the ousted partners had allegedly transferred assets to other businesses they controlled.³⁵ Those allegations -- serious but at this point in time, unproven -- apparently prodded BPA to reexamine its \$226-million curtailment agreement with Longview Aluminum.

BPA Discovers a Contract Provision

In December 2001, BPA wrote Longview Aluminum, saying it had “inadvertently overlooked” a provision in the \$226-million curtailment agreement. The overlooked provision, however, was not an obscure part of the contract. It was the provision that required Longview Aluminum to provide BPA with written notice promptly after withdrawing BPA money from the “company proceeds account.” In the nine months since signing the agreement, Longview Aluminum had not done so.

BPA now asked Longview Aluminum for the first time to document its expenditures. By then, BPA had paid the company almost 90% of the \$226 million in curtailment payments. BPA’s money had already gone out the door.



Longview Aluminum did not respond immediately because it wanted documents submitted to BPA to remain secret. To solve the problem, BPA and Longview Aluminum signed a confidentiality agreement in January 2002, obligating BPA not to disclose the company's financial information to anyone.³⁶

Even then, Longview Aluminum balked at providing information to BPA. So BPA wrote the company once again:

"It is impossible for BPA to determine at this time if Longview has used curtailment revenues consistent with the Curtailment Agreement."

Finally, in February 2002, Longview Aluminum sent BPA a chart listing its expenditures but only with a one or two-word description -- not enough for BPA to tell whether the expenses were consistent with the BPA contract. BPA asked for more information about several expenditures, including the repayment of loans from Longview Aluminum to affiliates of McCook and other companies.

Meanwhile, the trade press reported allegations of financial dealings at

McCook that should have put BPA on notice there were problems in the McCook corporate empire. GECC (the largest creditor of McCook) sued former board chairman Lynch and several other owners in federal district court, alleging fraud and misappropriation of McCook's corporate assets. GECC said McCook had purchased life insurance policies for Lynch and the other defendants, paid for a private limousine and chauffeur for Lynch, spent \$50,000 on a private dinner party at Lynch's house, spent another \$18,000 on a resort used by Lynch in Hawaii, and paid for \$56,000 to buy jewelry for Lynch.³⁷

Yet BPA appears to have done nothing more, except wait for Longview Aluminum to send more information. Even though the company had not fully responded to BPA's requests showing how it spent BPA money, BPA inexplicably sent it the last check of \$14.6 million in February 2002.

But BPA's check did not end its relationship with Longview Aluminum: the company now had an obligation to BPA to buy power again for half

the smelter. Longview Aluminum was supposed to notify BPA in April 2002 that it would begin operations with its refurbished "state of the art" facility. This was, after all, the point of BPA's lucrative payments. BPA had paid the extra money to the company so it could retrofit the aging smelter and keep jobs in the region.

In 2002, Longview Aluminum abruptly announced it would lay off 800 workers, the bulk of the work force.

Longview Aluminum was supposed to phase in production of aluminum by using 100 MW per month from BPA and then increasing its power usage three months later. "We can operate at 100 MW for three months with no problem," former BPA Administrator Hardy, a consultant to Longview Aluminum, told the utility trade publication *Clearing Up*. Hardy said Longview Aluminum was not affected by McCook's bankruptcy. Longview Aluminum was a separate firm with no debt, Hardy said, though he acknowledged the company "did not have a lot of capital."³⁸

Three weeks later, Longview Aluminum announced it would lay off 800 workers -- the bulk of the work force -- at the smelter. For the workers, Longview Aluminum's announcement was a double blow: they would not receive salary and benefits for the last three months of the curtailment period, as both BPA and the company promised, and they would not have jobs waiting them on July 1, 2002, as both BPA and the company promised.

Members of Congress Request an Audit



The layoffs prompted three members of Washington State's Congressional delegation to act.

On May 18, 2002, Senators Patty Murray and Maria Cantwell and Rep. Brian Baird (*left to right in photo*) wrote U.S. Secretary of Energy Spencer Abraham, asking him to audit Longview Aluminum and investigate whether the company met

its obligations to workers and BPA.

"This is turning out to be a story of promises made and promises broken," Sen. Cantwell said in an accompanying press release. "The public has a right to know the true story of McCook's intentions, what it has done with ratepayer's money, and what legal options are available to hold it accountable."³⁹

The letter requested Energy Secretary Abraham to make the results of the McCook audit public, and it posed four questions for him to answer:⁴⁰

- Was the initial sale of the Longview smelter from Alcoa to McCook predicated on a commitment to produce aluminum?
- Did McCook accurately represent its intentions to restart the plant in negotiating contracts with BPA? The letter asked for details about the extent of BPA's or the U.S. Department of Energy's review of McCook's financial status prior to entering into the contract.
- Did McCook honor its commitment to BPA and the workers?
- What legal remedies

are available to BPA or DOE to hold McCook accountable to its contractual obligations?


BPA Administrator Wright's answer to Congress was neither complete nor candid.

Energy Secretary Abraham forwarded the Congressional letter to BPA for response.

On June 25, 2002, BPA Administrator Wright answered. BPA was "very concerned about reports that Longview [Aluminum] may not be complying fully with its commitments" to workers, Wright said. But Wright made no commitment to do anything about the problem. Longview Aluminum, Wright insisted, had stated its intention to restart the smelter, but he did not explain how it would do that after laying off its employees.

Wright acknowledged that BPA "did not conduct an extensive financial review" prior to signing the \$226-million contract in 2001.

Nonetheless, Wright assured the members of



Congress that BPA was in the process of reviewing Longview Aluminum's use of BPA money "to ensure those proceeds were used for approved purposes. Longview has been very slow to respond to BPA's requests for information," Wright said. But he promised: "We will do everything possible to make the findings public."

Unfortunately, Wright's answer was neither complete nor candid. He made no mention of BPA's last payment of \$14.6 million to Longview Aluminum -- sent in February 2002 when BPA still had not received satisfactory answers to questions about what the company did with prior BPA payments.

Nor did Wright disclose that five months earlier, BPA had signed a confidentiality agreement with Longview Aluminum that precluded BPA from divulging Longview Aluminum's financial information and made release of the audit results difficult, if not impossible.

The Sham Audit

For reasons that have never been explained, BPA limited the scope of the audit and put it on a

fast track. On August 28, 2002, as the audit was nearing completion, BPA briefed Congressional staff about the preliminary results.

Although BPA was still in the dark about how Longview Aluminum spent BPA's money, BPA told Congressional staff it had uncovered no serious problems.⁴¹

If BPA wanted to deflect Congressional calls for a full accounting of the money, it succeeded. There is no record that any member of Congress (or the U.S. Department of Energy) ever inquired about the subject again.

BPA limited the scope of the audit and put it on a fast track.

Only in 2005 and 2006 was BPA forced to reveal the actual results of the audit -- documents that show unnamed officials in BPA management limited the inquiry and rendered it ineffective. But that is jumping ahead of the story.

On March 4, 2003, almost two years to the day after the BPA press conference

touting all the things that Longview Aluminum would do with BPA's money, the company filed for Chapter 11 protection under federal bankruptcy laws.⁴² Longview Aluminum joined McCook and other affiliates that had filed bankruptcy petitions in the preceding months.

American Metal Market, a trade journal, quoted an exasperated BPA press officer as saying Longview Aluminum board chairman and CEO Michael W. Lynch had "put \$75 million in his own pocket" as part of the BPA transaction.⁴³

Lynch responded furiously, and BPA was forced to clarify the statement. In a press release dated March 7, 2003, BPA said:

"BPA would like to clarify this statement to avoid any misunderstanding. Neither Mr. Hansen [the BPA spokesman] nor anyone at BPA wished to state or imply that Mr. Lynch personally 'pocketed' money paid to Longview by BPA....References to Mr. Lynch in that sentence were intended as references to Longview Aluminum, LLC."⁴⁴

BPA's press release added: "Not included in the [*American Metal Market*]



story was the fact that BPA has conducted a review of Longview Aluminum's uses of \$226 million BPA paid to the firm for not taking its contracted supply of power for a period of time. The review confirmed that Longview Aluminum's uses of the funds were in accord with its agreement with BPA.⁴⁵

But BPA's clarifications only raised more questions. If BPA believed Longview Aluminum had "pocketed" \$75 million, then its review (audit) of the files could not have showed the Longview Aluminum spent the money in accord with its BPA contract. It was one or the other. What was the truth?

Nor did a longer article in *The Oregonian* newspaper in 2004 shed much light on what happened to BPA's money. The article quoted BPA Administrator Wright as saying, "I don't regret any of the decisions [during the 2000-2002 energy crisis]. This power crisis was unprecedented and unanticipated. I think we did a good job under the circumstances." BPA spokesman Ed Mosey said: "You had a guy like Lynch [company board chairman Michael W. Lynch] who lined his pockets largely due to serendipity."⁴⁶

Later that year, the Longview bankruptcy trustee sold the smelter for scrap for a paltry \$2.5 million.⁴⁷ Only three years earlier, Longview Aluminum had paid \$140 million plus fees -- with BPA money -- for the plant. The smelter had produced not one pound of aluminum since Longview Aluminum acquired it.

The Bankruptcy Court Opinion

In 2005, a federal bankruptcy court in Illinois concluded that McCook was insolvent when it first approached BPA for help to buy the Longview smelter from Alcoa.⁴⁸ To avoid McCook's creditors, board chairman Lynch and several owners of McCook fraudulently transferred the \$226-million BPA curtailment agreement from McCook to a new company, Longview Aluminum, the court said. As a result, Lynch and the others owed money -- the profit made at Longview Aluminum -- to McCook and its creditors.⁴⁹

More information also came out in 2005 about Longview Aluminum's relationship with former BPA Administrator Hardy. The bankruptcy trustee filed claims against numerous law firms and

consultants to recover money paid by Longview Aluminum. One of the defendants was the Hardy's firm, Hardy Energy Consulting, which received \$326,000 between 2001 and 2003, according to the trustee. Hardy's firm ultimately settled the case for an unknown amount without admitting any of the allegations.⁵⁰

BPA Releases Some Records

BPA was forced to release some documents, too, in 2005 and 2006. In response to Freedom of Information Act ("FOIA") requests from the bankruptcy trustee's law firm and the author of this article, BPA made public the audit conducted at the requested of members of Congress.

BPA's records show that unnamed officials at BPA instructed the audit staff to conduct only a limited examination in 2002 of Longview Aluminum's expenditures, not a comprehensive investigation, as requested by Senators Cantwell and Murray and Representative Baird.

On September 12, 2002, BPA's audit staff -- in an unsigned statement, not on BPA letterhead but on plain

white paper -- explained the constraints under which they operated:

"[W]e reviewed and selectively tested expenditure schedules, invoices, other documentation, and bank statements (provided by Longview) to verify that the records were mathematically correct and internally consistent....



"While we found no evidence indicating that the original expenditure records and documentation had been tampered with, our records and documentation review was restricted to examining photocopies of the assumed original documents and records. Further, we could not make direct inquiries with Longview's officers regarding expenditures."⁵¹

Who restricted the BPA audit staff in this way? We do not know. BPA work papers -- labeled

"FRED's AUDIT FILE" -- show that BPA audit staff only reviewed Longview Aluminum's files to make sure the company wrote checks that matched the amount on the invoice. BPA did not analyze whether its money was spent for qualified expenditures under the \$226-million contract. But that was precisely what the members of Congress said they wanted to learn.

The audit staff noted: "It is our understanding that BPA AE [account executive] (Mr. Mark Miller) has concluded that these expenditures qualify under Section 10 of the contract." Nothing more was said.⁵² The files contain no further documentation.

A cursory examination of BPA's audit files, however, shows that BPA still did not understand what happened to its money and had good reason to pursue a full audit, as the members of Congress had requested in the first place.

Longview Aluminum, for example, disclosed in July 2002 that it had used \$7.8 million in BPA funds to pay McCook's debts, including the cost of the initial anti-trust lawsuit filed against Alcoa in May 2000.⁵³

Other debts appear unrelated to the smelter. Longview Aluminum, for instance, paid \$2.2 million to Samuel & Co., a creditor of McCook, even though these obligations were incurred in 1999, two years before BPA signed the curtailment agreement with Longview Aluminum.⁵⁴

Records also show that Longview Aluminum spent \$372,000 for life insurance policies for its executives at the same time the company was laying off workers at the smelter. Those expenses are a small percent of what the company ultimately received from BPA, but why did they not trigger a more thorough review?

Other FOIA requests to BPA yielded little useful information, though federal records law requires BPA (and other agencies) to retain business records for years, sometimes for decades. The absence of BPA records suggests BPA never obtained essential records in the first place or it subsequently destroyed documents relating to McCook and Longview Aluminum.

BPA, for example, said it had no communications at all with McCook or Longview Aluminum



showing how it established the \$226 million-amount.⁵⁵ If BPA is to be believed, the number was picked out of thin air with no analysis. Furthermore, BPA did not inform the U.S. Department of Energy prior to signing the \$226-million curtailment agreement.⁵⁶



Nor did BPA analyze McCook's or Longview Aluminum's finances, assets and long-term viability prior to BPA signing the \$226-million curtailment agreement. If BPA's response is accurate, BPA never requested a bank statement or balance sheet from either McCook or Longview Aluminum.⁵⁷

Finally, BPA said it had few, if any, meaningful documents with former BPA Administrator Hardy. Hardy, who served as one of McCook's and Longview's key representatives, neither received nor submitted written documents or e-mails to BPA in exchange for earning \$326,000 from Longview Aluminum over a two-year period.

Reassessment

BPA's money is gone, even though the bankruptcy proceedings for McCook and Longview Aluminum continue to this day.

The total price tag for Longview transaction now approaches \$292.5 million. In addition to the \$226 million that BPA spent on the curtailment agreement, the federal government claims it is owed \$66.5 million by the bankrupt company. The U.S. Pension Benefit Guaranty Corp., an independent government entity created to pay worker pensions in case of corporate default, is Longview Aluminum's largest creditor. The PBGC asserts that it is owed \$30 million. BPA is a creditor, too. Longview Aluminum still owes it \$33.5 million from unpaid power and transmission bills, as well as liquidated damages under the five-year power sales contract when Longview Aluminum did not restart the smelter.

Meanwhile, the Longview bankruptcy trustee has sued Alcoa in Cowlitz County Superior Court, alleging that it knew McCook and Longview could not run the smelter profitably.⁵⁸

Michael W. Lynch's legal problems continue to mount. In 2005, a federal district court judge in Illinois found that Lynch fabricated a document attempting to shift his liability on a \$30-million personal loan to a company, McCook Properties. The transaction was unrelated to BPA or Longview Aluminum. The court said Lynch lied on the stand in a civil trial when he argued the loan was not his individual responsibility to repay. "The evidence made clear that Lynch fabricated the documents, and Lynch, and Lynch alone, ultimately decided to offer his perjured and false testimony," the court concluded.⁵⁹

Lynch, unable to pay the note, filed for individual bankruptcy in 2005. He continues to pursue civil litigation against various lawyers, judges and others, alleging a broad conspiracy to deprive him of his livelihood.⁶⁰ In 2006, he filed legal papers in federal court alleging evidence of a "bribery fund" used by companies and law firms to pay judges in Chicago to rule against him.⁶¹

Then, in October 2006, a Cook County judge in Chicago sentenced Lynch to jail for 60 days for criminal contempt after



Lynch accused the judge (and others) of having received mob money. The newspaper in Longview had this to say: "Arguably one of the most hated men ever to set foot in Cowlitz County is behind bars in Cook County, Illinois."⁶²

What would have happened if McCook had never approached BPA in 2000? The Longview smelter would almost certainly have remained in Alcoa's hands. Had BPA paid Alcoa what it paid other smelters in 2000-2002 to curtail power usage, BPA would have written a check for \$75 million (not \$226 million) to shut down during the energy crisis.

Whether Alcoa would have restarted part or all of the smelter in 2002 is not known, though some union leaders believe Alcoa would have closed the Longview smelter permanently -- all of it. "There's no doubt in my mind that Alcoa would have shut down the north and the south plants," said Wes Wheeler, the veteran worker and head of the Longview Federated Aluminum Council. Wheeler, 51, now works as a pharmacy technician.

Wheeler said Alcoa did well for itself in the transaction.

It received \$150 million from Longview Aluminum (BPA money) for a smelter that it did not want to keep operating anyway. In addition, Alcoa also relieved itself of having to pay pensions and medical benefits to the workers -- an obligation that Longview Aluminum assumed and then broke when it went into bankruptcy.

Wheeler, who was eligible for early retirement in 2001 when Longview Aluminum purchased the smelter, said he lost his medical benefits and will collect only 40% of his retirement from the U.S. Pension Benefits Guaranty Corporation until he turns 60. Other long-time workers are in the same position. Meanwhile, the Longview smelter has been gutted -- the buildings stand idle and empty.

"BPA has a tremendous amount of authority, the ability to make a meaningful and positive difference in people's lives, and a statutory framework that requires sound business operations combined with a commitment to serve the public interest," Administrator Wright recently told *Electric Light & Power* magazine, describing why he has a "dream job." BPA, he said, is "a unique combination of

public sector and private sector that I have always found energizing."⁶³

But an executive in the private sector who mismanages tens of millions of dollars, as BPA did under Wright's tenure, rarely holds on to his or her job. There is some degree of accountability for shareholders and board members. BPA, however, has no board of directors and no shareholders: it reports to the Secretary of Energy, who traditionally has taken a hands-off approach to the agency.

Questions

In the end, we are left with more questions than answers about BPA's curious relationship with Longview Aluminum.

1. Why did BPA sign the \$226-million curtailment contract with Longview Aluminum, a company with no assets and whose affiliate, McCook, could not secure a normal loan to buy the smelter from Alcoa?

2. Why did BPA pay Longview Aluminum three times more (per MWh) than what other aluminum smelters received for shutting down during the 2000-2002 energy crisis?

The answers to those questions still matter -- even now.

3. Why did BPA conduct no financial “due diligence” on McCook and Longview? Did BPA Administrator Wright know he was dealing with a company that was insolvent (McCook) and another company (Longview Aluminum) with no assets? If so, why?

4. Why did BPA tell members of Congress and the press that BPA had discovered no improprieties in the 2002 audit of Longview Aluminum when, in fact, the audit (and documents submitted to BPA prior to the audit) appear to show expenditures of funds for unauthorized purposes?

5. Why did BPA make no attempt to recover money from Longview after it learned of questionable expenditures?

6. What happened to BPA’s records? Among the missing records are those showing the role of former BPA Administrator Randy Hardy, who negotiated and then helped implement the McCook/Longview Aluminum transaction. Why did Hardy’s activities leave no paper trail at BPA?

BPA has embarked on a process to sign new 20-year contracts next year with all of its customers, including utilities and the remaining aluminum smelters. Can customers trust BPA to be a good business partner? Who will watch BPA when the new contracts are in place? If a transaction worth a quarter billion dollars does not inspire a complete, candid response by BPA to Congress, when? Without additional oversight, what is to prevent BPA from engaging in the same type of conduct again? What redress will customers have if history repeats itself?



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ENDNOTES

1. McCook purchased \$200 million per year in raw materials from the Reynolds smelter in Longview. McCook, in turn, supplied aluminum for the Lockheed-Martin F16 fighter jet, NASA Space Shuttle and wing skins for the Boeing C-17 plane, among others. Source: *Price et al v. Seventh Circuit Court of Appeals*, 5:2006cv04055, U.S. District Court of Kansas.
2. *McCook Metals LLC v. Alcoa*, 1:2000cv01011, U.S. District Court, District of Columbia. McCook had sued Alcoa in the past over other issues. In June 1999, for example, McCook sued Alcoa in federal district court alleging that Alcoa interfered with McCook's customers and monopolized products in violation of the Sherman Act. Two of Alcoa's patents for making high-strength aluminum were neither valid nor enforceable, McCook's complaint alleged. *McCook v. Alcoa*, 1:99-cv-03856. *McCook Metals, L.L.C. v. Alcoa*, 249 F.3d 330 (4th Cir. 2001).
3. *In re McCook Metals L.L.C.*, 319 B.R. 570, 579 (Bkrctcy.N.D.Ill. 2005).
4. *Id.* at 578.
5. The bankruptcy court in Illinois in 2005 concluded: "Continuing uncertainty about energy prices prevented McCook from obtaining conventional financing for the Longview smelter acquisition, even though it approached several lenders." *Id.* at 580.
6. Another company, Vanalco, which owned a smelter in Vancouver, Washington, also cut production by 80% in June 2000 and closed the remaining part of its smelter in September 2000.
7. See statement of former BPA Administrator Randy Hardy, as recorded in the minutes of the Northwest Aluminum Industry Study Group, November 17, 2000 (p.7).
8. See BPA response to Freedom of Information Act ("FOIA") request 05-051 at page 43. BPA's FOIA responses are posted on its web site and can be downloaded from the site. www.bpa.gov/corporate/public_affairs/FOIA/Reading_Room.cfm
9. *Id.* at 43.
10. *Id.* at 43.
11. *Id.* at 44.
12. BPA's five-year power sales contracts began a year later, on October 1, 2001 (FY 2002).
13. Initially, Wright was named "Acting Administrator," an interim appointment. Wright was named permanent Administrator in February 2002. For purposes of this article, the author refers to him simply as "Administrator," though he served for roughly 15 months as interim head of the agency.
14. BPA sells power from 31 federal dams and other sources, including a nuclear power plant in Washington State and various wind energy facilities. See "About BPA" tab at www.bpawatch.com for details.
15. BPA faced unexpected returning load from both public power utilities and other smelters, who wanted to buy BPA power as market prices rose rapidly.
16. BPA proposed to "buy back" its contract obligations under the remaining months of the 1996 contracts with the aluminum smelters (which expired September 30, 2001) and some months under the new contracts (which began October 1, 2001). Typically, the total curtailment period lasted between one and two years.
17. In a single transaction with a smelter, BPA could curtail the same amount of power consumed by a small city. The Longview smelter, for example, consumed 480 aMW of power (roughly 5.2 million MWh a year). BPA also sought to "buy back" commitments to sell power to utility customers. BPA said these curtailment agreements (also called "load reduction" contracts) were necessary if BPA were to avoid imposing a 250% rate increase to pay for expensive power.
18. See lobbying records for O'Keefe, Ashenden, Lyons and Ward. Also, see

- lobbying records for the Patton Boggs firm. <http://www.sopr.senate.gov>
19. Longview Aluminum LLC incorporation papers, filed with the Secretary of State in Washington, #0-1367903, December 27, 2000.
 20. Records show that 99% of Longview Aluminum's operating income for 2001 came from BPA. As of February 26, 2001, when BPA signed the \$226-million curtailment contract, Longview Aluminum had \$3.2 million in cash and no other tangible assets. See Memorandum of Decision, page 13 (July 14, 2005), in bankruptcy case 03-B-12184, U.S. Bankruptcy Court, Northern District of Illinois.
 21. McCook press release, December 27, 2000. The press release referred to McCook's "parent company," Michigan Avenue Partners, as being the signing entity. The press release said the agreement was "contingent on financing." In fact, the signing entity was Longview Aluminum LLC ("Longview Aluminum").
 22. BPA press release, March 1, 2001, "BPA inks an innovative aluminum agreement with McCook Metals" (PR14).
 23. *Id.* In its March 1, 2001 press release, BPA asserted that the "buy-back" price paid to McCook was less than half the market price. This assertion is undocumented. In response to a Freedom of Information Act ("FOIA") request in 2005, BPA said it had no information showing how it established the \$226-million price. See BPA response to FOIA #06-03. An internal BPA document dated March 1, 2001 ("Talking Points") said market prices had reached \$275-\$380 per MWh "and sometimes soar well over \$700 per MWh." But those prices were typically for short-term transactions, not long-term (i.e., 16-month) arrangements for large quantities of power. BPA could have ascertained the true costs of supplying Longview Aluminum by requesting a bid from utilities and power marketers. The bid would have served as a proxy -- a benchmark -- by which BPA could evaluate whether its curtailment payments represented a "savings" to the region. There is no record BPA ever took such a step.
 24. The utility trade publication *Clearing Up* (March 5, 2001, page 8) quoted Lynch as saying McCook would build 1,100 MW of new turbines and that improvements to the smelter with "cutting-edge nanotechnology" would reduce power needs by half.
 25. The best documentation for the \$20-per MWh amount paid to other DSIs is contained in an affidavit dated May 14, 2002, and submitted by BPA vice president Stephen Oliver to the U.S. Court of Appeals for the Ninth Circuit in response to a petition challenging the legality of BPA's "buy back" (curtailment) agreements with the DSIs. The court ruled in BPA's favor. *Bell v. BPA*, 340 F.3d. 945 (9th Cir. 2003). At issue in the lawsuit was whether BPA had the legal authority to sign the contracts. The court did not address the management issues and history described here. The \$20-per MWh amount was also reported in the trade press. See, for example, *Clearing Up* on September 24, 2001.
 26. Michigan Avenue Partners, the "parent" of McCook, signed a contract with the smelter's chief union, the United Steelworkers of America, obligating itself to contribute \$35 million. It never did so. Even that sum, however, was a small amount compared with the total cost of retrofitting the smelter and building a new power plant -- an expense of several hundred million, perhaps even \$1 billion.
 27. Section 10 of the BPA curtailment agreement with Longview Aluminum L.L.C., #01PB-10786.
 28. Section 10 of the BPA-curtailment agreement with Longview Aluminum LLC created four general categories of qualified expenditures:
 - a) curtailment and other costs, such as cost of cancellation penalties for alumina and other materials;

- b) power, upgrades to the smelter and job retention costs, as well as expenditures for planning, licensing, siting and building a power plant;
 c) taxes; and
 d) loan proceeds, including the principal, interest, fees and other costs associated with the smelter acquisition.
29. Section 10(g).
30. *Longview Daily News*, March 3, 2001.
31. *Longview Daily News*, March 29, 2001.
32. *In re McCook Metals L.L.C.*, case #01-27326, U.S. Bankruptcy Court, Northern District of Illinois.
33. Lynch said he needed to leave McCook in order to make a bid to buy its assets and bring the company out of bankruptcy. In order to avoid a conflict-of-interest, he relinquished his corporate responsibilities with McCook while still retaining them at Longview Aluminum.
34. *American Metal Market*, October 29, 2001.
35. *GECC et al v. Michael Lynch et al*, 1:2002cv01185, U.S. District Court for the Northern District of Illinois, Eastern Division, February 20, 2002.
36. See BPA response to FOIA #06-003.
37. See the GECC litigation cited above in footnote 35. A summary of the allegations was reported in *American Metal Market*, March 1, 2002.
38. *Clearing Up*, March 25, 2002. To say that Longview Aluminum did not have any debt was technically true but missed the point. The company had no debt because BPA had paid it.
39. See Sen. Cantwell's web site, <http://cantwell.gov/news>.
40. The use of the name "McCook" suggested that the members of Congress did not know BPA's \$226-million contract was with Longview Aluminum, a shell corporation set up specifically to receive BPA money and own the smelter.
41. No written materials were provided to Congressional staff. Source: phone interview with BPA account executive Mark Miller on September 26, 2006. Miller's comments are consistent with internal BPA e-mails that refer to BPA concluding that Longview Aluminum spent BPA funds in accordance with the contract.
42. *In re Longview Aluminum L.L.C.*, case #03-12184, U.S. Bankruptcy Court, Northern District of Illinois.
43. *American Metal Market*, March 6, 2003.
44. BPA press release 10-03, "BPA clarifies statement regarding Longview Aluminum," March 7, 2003.
45. *Id.*
46. *The Oregonian*, April 11, 2004. "BPA Deal Meets Goal at Big Cost."
47. *Longview Daily News*, February 10, 2005.
48. *In re McCook Metals L.L.C.*, 319 B.R. 570 (Bkrtcy.N.D.Ill. 2005). "By December 31, 2000, McCook was insolvent, unable to pay its debts as they became due, and was engaging in business with unreasonably small amounts of capital...". *Id.* at 578.
49. *Id.* at 599.
50. See filings in bankruptcy case, *In re Longview Aluminum, L.L.C.*, #03-12184. The amended complaint against Hardy Energy Consulting was filed on January 6, 2005, and was settled on April 4, 2005.
51. BPA response to FOIA #06-0012 at page 76. The audit files are found at pages 77-92.
52. *Id.* at 76. Miller is not in BPA executive management. Internal correspondence at BPA from this time period showed that BPA's Office of General Counsel and BPA vice president Stephen Oliver were informed about matters pertaining to Longview Aluminum, but it is not known who restricted the audit.
53. Longview Aluminum explained on July 31, 2002 -- for the first time -- that it had signed a note on February 27, 2001, shortly after the BPA curtailment contract went into effect, obligating itself to pay \$7.8 million ("the term note") to McCook. The note itself did not divulge why

- Longview Aluminum owed this money to McCook. In the July 31, 2002 letter, Longview Aluminum explained that the note was “intended to memorialize an obligation of Longview to pay McCook for certain payments which McCook had advanced to third parties on behalf of Longview relating to the acquisition [of the smelter]...”. The transfer of money from one affiliate to another should have prompted BPA to ask for more information, but there is no record that BPA did so. Instead, BPA appears to have just closed the matter.
54. McCook owed money to Samuel & Company stemming from a patent dispute dating back to 1999. Longview paid \$2.2 million to the company which was considered an “offset” against McCook’s obligations.
55. BPA response to FOIA request #06-003. The author of this article asked for all communications between BPA and Longview Aluminum and its agents (i.e., lawyers and consultants) regarding the amount
- to be paid by BPA to the company and how the final amount (\$226 million) was justified and established. On December 1, 2005, BPA said it was “unable to locate any communications” in response to this inquiry.
56. *Id.*
57. BPA response to FOIA #06-0012.
58. See records in the Superior Court of Cowlitz County, Washington. *Brandt v. Alcoa*, 05-2-00355-4.
59. *REP MCR Realty LLC v. Michael Lynch*, 363 F.Supp.2d 984, 1016 (N.D. Ill. 2005).
60. See, for example, *Price et al v. Seventh Circuit Court of Appeals*, 5:2006cv04055, U.S. District Court of Kansas.
61. *Forbes*, May 31, 2006. Michael W. Lynch, former chairman of McCook Metals, filed legal papers in Chicago Federal Court disclosing the judicial “Bribery Fund” uncovered during the McCook Metals bankruptcy proceedings.
62. *Longview Daily News*, October 17, 2006.
63. *Electric Light and Power*, July - August 2007, page 4.