

**STATE OF CONNECTICUT
BEFORE THE DEPARTMENT OF PUBLIC UTILITY CONTROL**

**Application of Connecticut Light & Power)
and United Illuminating for Approval of)
Nuclear Generation Assets Divestiture Plan)**

Docket No. 99-09-12

**DIRECT TESTIMONY OF
PAUL CHERNICK
ON BEHALF OF
THE OFFICE OF CONSUMER COUNSEL**

Resource Insight, Inc.

JANUARY 18, 2000

This testimony has been redacted to remove confidential information.

TABLE OF CONTENTS

I. Identification and Qualifications 1

II. Introduction and Summary 3

III. The Market for Nuclear Assets 5

 A. Market Maturity..... 5

 B. Demand and Supply..... 8

IV. Plant-specific Considerations in the Timing of the Millstone Sale..... 13

 A. The Millstone 3 Joint Owners 14

 B. Millstone and Seabrook..... 21

 C. Ongoing Litigation 22

 D. Millstone operating risks 23

 E. Shareholder Incentive and Ratepayer Benefits 23

EXHIBITS

Exhibit PLC-1

Professional Qualifications of Paul Chernick

1 **I. Identification and Qualifications**

2 **Q: State your name, occupation and business address.**

3 A: I am Paul L. Chernick. I am the president of Resource Insight, Inc., 347
4 Broadway, Cambridge, Massachusetts 02139.

5 **Q: Summarize your professional education and experience.**

6 A: I received an SB degree from the Massachusetts Institute of Technology in
7 June, 1974 from the Civil Engineering Department, and an SM degree from
8 the Massachusetts Institute of Technology in February, 1978 in technology
9 and policy. I have been elected to membership in the civil engineering
10 honorary society Chi Epsilon, and the engineering honor society Tau Beta Pi,
11 and to associate membership in the research honorary society Sigma Xi.

12 I was a utility analyst for the Massachusetts Attorney General for more
13 than three years, and was involved in numerous aspects of utility rate design,
14 costing, load forecasting, and the evaluation of power supply options. Since
15 1981, I have been a consultant in utility regulation and planning, first as a
16 research associate at Analysis and Inference, after 1986 as president of PLC,
17 Inc., and in my current position at Resource Insight. In these capacities, I
18 have advised a variety of clients on utility matters. My work has considered,
19 among other things, power supply planning, rate design, cost allocation, and
20 utility industry restructuring. My resume is appended to this testimony as
21 Exhibit PLC-1.

22 **Q: Have you testified previously in utility proceedings?**

23 A: Yes. I have testified approximately one hundred and fifty times on utility
24 issues before various regulatory, legislative, and judicial bodies, including the

1 Massachusetts Department of Public Utilities, Massachusetts Energy
2 Facilities Siting Council, Vermont Public Service Board, Maine Public
3 Utilities Commission, Rhode Island Public Utilities Commission, Texas
4 Public Utilities Commission, New Mexico Public Service Commission,
5 District of Columbia Public Service Commission, Michigan Public Service
6 Commission, Minnesota Public Utilities Commission, Public Utilities
7 Commission of Ohio, South Carolina Public Service Commission, North
8 Carolina Utilities Commission, Florida Public Service Commission,
9 Pennsylvania Public Utilities Commission, New York Public Service
10 Commission, Arizona Commerce Commission, New Orleans City Council,
11 Federal Energy Regulatory Commission, and the Atomic Safety and
12 Licensing Board of the U.S. Nuclear Regulatory Commission. A detailed list
13 of my previous testimony is contained in my resume.

14 **Q: Have you testified previously before this Commission?**

15 A: Yes. I testified in

- 16 • Docket No. 83-03-01, a United Illuminating (UI) rate case, on behalf of
17 the Connecticut Consumers Counsel, on Seabrook costs.
- 18 • Docket No. 83-07-15, a Connecticut Light and Power (CL&P) rate case,
19 on behalf of Alloy Foundry, on industrial rate design.
- 20 • Docket No. 99-02-05, the CL&P stranded-cost docket.
- 21 • Docket No. 99-03-04, the UI stranded-cost docket.
- 22 • Docket No. 99-03-35, the UI standard-offer docket.
- 23 • Docket No. 99-03-36, the CL&P standard-offer docket.
- 24 • Docket No. 99-08-01, the investigation into electric capacity and
25 distribution.

26 **Q: Have you previously worked in other capacities before this Commission?**

1 A: Yes. I assisted the DPUC staff, including conducting cross examination, in
2 Docket No. 87-07-01, Phase 2, in the period March 1988 to June 1989. I also
3 provided training to the DPUC staff on cost allocation in 1993.

4 **II. Introduction and Summary**

5 **Q: On whose behalf are you testifying?**

6 A: I am testifying on behalf of the Office of Consumer Counsel (OCC).

7 **Q: What is the purpose of your testimony?**

8 A: I address a number of issues related to the timing of the Millstone asset sale
9 proposed by Connecticut Light and Power (CL&P), which United
10 Illuminating (UI) has joined.

11 **Q: Please summarize your conclusions.**

12 A: As I have testified in a number of other proceedings, the best way to
13 determine stranded costs of generation assets is through a properly-structured
14 auction. Part of the structuring of an auction is its timing. My primary
15 conclusions with regard to the timing of the Millstone sale are as follows:

- 16 1. The market price of Millstone is likely to be increased if
- 17 • The sale includes a greater share of total ownership (ideally
 - 18 100%).
 - 19 • The minority owners' rights of first refusal are eliminated prior to
 - 20 the auction.
 - 21 • The Millstone 3 joint owners have reached consensus regarding the
 - 22 process for evaluating bids and allocating proceeds between Units
 - 23 2 and 3.

- 1 • The OCC's appeal of the minimum bid is resolved prior to the
2 auction.
- 3 • Additional nuclear purchasers have entered the market.
- 4 • The sale is timed to avoid the wave of near-term nuclear
5 divestitures Mr. McWhinney identifies.
- 6 • PECO (half the AmerGen joint venture) has concluded its merger
7 with Unicom.
- 8 • Northeast Utilities (NU) has an opportunity to demonstrate that
9 Millstone has emerged from the regulatory cloud under which it
10 has operated since the shutdown of all three units in 1996.
- 11 • Millstone is sold jointly with Seabrook, allowing the buyer to
12 benefit from the synergies of operating the very similar Seabrook
13 and Millstone 3 units.
- 14 2. The inclusion of CMEEC's share of Millstone 3 in the auction would
15 increase the value of the plant to CMEEC customers.
- 16 3. The aggressive schedule CL&P has proposed for the Millstone sale is in
17 the interests of shareholders, but not of ratepayers.

18 **Q: What are your recommendations to the Commission in this proceeding?**

19 A: I recommend that the Commission reject the proposal, as to the timing of the
20 sale. The Commission can keep this docket open to address issues of the
21 auction design, and require regular (perhaps semi-annual) reports from the
22 utilities regarding the state of the market and resolution of the plant-specific
23 issues listed in my previous response.

24 The market and conditions are Millstone may make it appropriate to
25 start the auction process as soon as early 2001, or as late as the end of 2002.

1 **III. The Market for Nuclear Assets**

2 **Q: What is CL&P's rationale for the proposed timing of the Millstone**
3 **auction?**

4 A: Supply and demand considerations represent CL&P's primary rationale for
5 the proposed timing of the sale. Mr. McWhinney also mentions issues of
6 market maturity and risk (which I address in §IV.D).

7 **Q: Do supply and demand considerations, or market maturity, argue for a**
8 **prompt auction of Millstone, rather than delay of the sale until later in**
9 **the interim period?**

10 A: No, as I explain below.

11 **A. Market Maturity**

12 **Q: What do you mean by "market maturity"?**

13 A: I refer here to a number of factors that affect the operation of the market for
14 nuclear-asset sales, including the number of purchasers, their experience with
15 the process of purchasing and assuming control of nuclear plants, and
16 resolution of regulatory and financial concerns.

17 **Q: Do you consider the market for nuclear-asset sales to be mature?**

18 A: No. Excluding purchases of minority ownership shares by other joint owners,
19 only two purchasers—Entergy and AmerGen—have been publicly identified
20 as being active in bidding on nuclear assets. Winning bidders have been
21 selected for only seven units at the following six plants:¹

¹The long lists of nuclear sales, such as that in Mr. McWhinney's Exhibit RTM-2, are dominated by the transfer to joint owners (usually the lead owner) of minority portions of Seabrook, Salem 1 and 2, Peach Bottom 1 and 2, Hope Creek, Beaver Valley 1 and 2, Perry, and River Bend. These transactions (ten of the seventeen units in Exhibit RTM-2) provide

- 1 • Pilgrim
- 2 • Three Mile Island 1
- 3 • Clinton
- 4 • Vermont Yankee
- 5 • Oyster Creek
- 6 • Nine Mile Point 1 and 2

7 Transactions have closed for only the first three units. As I will discuss
8 below, the Nine Mile Point sale is currently disputed.

9 **Q: Is this market much less mature than the market for fossil and hydro**
10 **generation assets?**

11 A: Yes. Fossil and hydro sales for operation in the competitive market started
12 earlier than the nuclear sales, and the market has been much more vigorous.
13 About two dozen companies have purchased hydro and/or fossil capacity,
14 representing over 300 units.

15 **Q: Does CL&P believe that the market is mature?**

16 A: No. Mr. McWhinney, CL&P's witness on this issue, testifies that the nuclear
17 asset market is immature (direct, p. 10).

18 **Q: Is the market likely to mature over the next couple of years.**

19 A: I believe so, and the evidence offered by CL&P supports this view.
20 According to CL&P, four entities have expressed interest in the Millstone
21 plant: AmerGen, Dominion, Entergy, and Duke (IR EL-010, AG-022).
22 According to Mr. McWhinney, seven entities (the Midwest Operating
23 Company, Constellation, and PP&L) have expressed interest in nuclear

valuable information about the market value of nuclear assets, but they are not good models for purchases of a majority share in a plant by party that is not a current joint owner.

1 acquisitions in general (IR AG-023).² These opinions are corroborated by the
2 president and COO of Dominion Resources (in an article in Standard &
3 Poor's Utilities and Perspectives, November 29, 1999), in which he states
4 that "In the coming months, ...additional buyers, including Dominion
5 Generation, will enter the market" (Attachment to IR OCC-108).

6 As noted above, only Entergy and AmerGen have actually purchased
7 nuclear units, and there does not appear to be any public evidence that any
8 other bidder has been a serious contender for any nuclear unit.³ If a large
9 fraction of the seven potential bidders were actually active in the Millstone
10 auction, the realized price would likely be higher than if only Entergy and
11 AmerGen are active. At this point, the evidence seems to be that more
12 bidders will enter the market over time.

13 Mr. McWhinney believes that "the market is maturing and will continue
14 to do so" (IR OCC 1-033). He also expresses the opinion that "Other nuclear
15 utilities can be expected to begin acquiring nuclear plants for fear of being
16 behind the two leading buyers" (Direct, p. 12).

²Mr. McWhinney also lists Unicom as a potential buyer; since it is merging with PECO, which is half of AmerGen, it is unlikely that both Unicom and AmerGen would be bidding on the same plant. Mr. McWhinney identifies two small utilities (Rochester Gas & Electric and Central Hudson Gas & Electric) as potential nuclear buyers, but they are probably too small to be interested in taking control of nuclear units, other than Rochester G&E's role as a proxy for Entergy, in exercising its right of first refusal for Nine Mile Point.

³The two nuclear buyers were reported to be in direct competition for Vermont Yankee; AmerGen won the auction for Nine Mile Point, but has apparently lost out to the exercise of Rochester Gas and Electric's right of first refusal, with Entergy to be the actual operator. Thus, of the eight publicly-identified efforts to obtain control of nuclear units, all eight involve just these two buyers.

1 The prospect of a maturing market, and hence more vigorous
2 competition between bidders, strongly suggests that delaying the sale would
3 be beneficial.

4 **Q: Is there any other reason to believe that the market will become more**
5 **competitive over the next couple of years than it is today?**

6 A: Yes. Both of the two established nuclear bidders are somewhat distracted at
7 this point. As I discuss below, Entergy is busy negotiating the acquisition of
8 the NYPA plants, and has indicated that it is interested in acquiring only a
9 few more units. The potential of AmerGen to pursue nuclear acquisitions in
10 the short term may be compromised by the distraction of PECO, which
11 represents half of AmerGen, with its acquisition of Unicom and its ten
12 nuclear units.⁴ AmerGen's nuclear acquisition plans represent the bulk of
13 such announced plans. A sale in 2000 may be the least advantageous timing.
14 Once the short-term distractions are resolved, and more purchasers enter the
15 market, the market should become more competitive.

16 ***B. Demand and Supply***

17 **Q: What is CL&P's position regarding the demand and supply for nuclear**
18 **assets?**

19 A: In his direct testimony, Mr. McWhinney argues that "now is a good time to
20 sell a nuclear plant" (direct, p. 12) because:

- 21 • "There is a group of buyers who are interested in nuclear plants and
22 who have the capabilities to properly manage and leverage the value of
23 larger fleets of nuclear plants" (direct, p. 12).

⁴CL&P has not evaluated the effect of the Unicom merger and other acquisitions may affect the ability of AmerGen to pursue extensive nuclear acquisitions in the short term.

- 1 • “Both of the two primary buyers of nuclear assets—Entergy and
2 AmerGen—have publicly stated their intention to buy considerably
3 more nuclear capacity in the near term” (IR OCC-023, OCC-100).
- 4 • “Other nuclear utilities can be expected to begin acquiring nuclear
5 plants for fear of being behind the two leading buyers” (direct, p. 12).
- 6 • “More nuclear plants, and especially minority interests in plants, will be
7 coming onto the market for sale. Hence, the increased supply of plants
8 onto the market is likely to dampen future purchase prices” (direct, p.
9 12).
- 10 • “Only a small number of nuclear plants of partial shares have been put
11 on the block relative to the number that are likely to be sold in the
12 future. Consequently, the supply of plants for sale is presently limited.”
13 (IR OCC-023, OCC-100).

14 **Q: Does CL&P’s evidence support his characterization of the market?**

15 A: No. To the contrary, the evidence that CL&P has offered in this case suggests
16 that

- 17 • The two active nuclear buyers are no more likely to purchase Millstone
18 in an auction in early 2000 than they are if the auction were in 2002.
- 19 • The other potential buyers have not yet entered the market.
- 20 • Based on CL&P’s analysis, there would appear to be short-term glut of
21 nuclear capacity on the market, so that delaying the sale a couple years
22 may improve the demand-supply balance.

23 **Q: Why do you say that the two active nuclear buyers are no more likely to
24 purchase Millstone in 2000 than in 2002?**

25 A: The only information CL&P has provided about the scope of the acquisition
26 plans of Entergy and AmerGen is in two articles attached to IR OCC-025.

1 The first article quotes Entergy as expecting “to purchase five to eight
2 additional nuclear plants...over the next several years.” The same article
3 notes that Entergy is currently negotiating the purchase of two plants from
4 the New York Power Authority, which would leave its target at three to six
5 plants. In any case, Entergy’s horizon of “several years” would cover the
6 Millstone auction, whether Millstone is auctioned as soon as feasible, or late
7 in 2002 (to allow the sale to close by the end of 2003, consistent with Public
8 Act 98-28). If Mr. McWhinney is correct about the amount of nuclear
9 capacity coming on the market, Entergy is planning on buying only a small
10 portion of it.

11 The second article quotes AmerGen as planning to acquire “up to
12 twenty US operating nuclear units.” Elsewhere, the same article identifies
13 AmerGen’s target date for acquiring twenty units as 2003. Thus, AmerGen
14 will be in the market for the Millstone purchase, either early or late. Its
15 acquisition goals are not likely to be fulfilled much before the Millstone sale
16 in any case.

17 **Q: Why do you say that CL&P’s evidence suggests that there is a short-**
18 **term glut of nuclear capacity on the market?**

19 A: CL&P’s witness Mr. McWhinney identifies the following units as being
20 “expected to sell in the near term:”

- 21 • Millstone 2 and 3,
- 22 • Seabrook,
- 23 • Indian Point 2,
- 24 • Indian Point 3,
- 25 • Fitzpatrick,
- 26 • Ginna,

- 1 • San Onofre 2 and 3,⁵
- 2 • Diablo Canyon 1 and 2,
- 3 • Palo Verde 1, 2, and 3,
- 4 • Quad Cities 1 and 2, and
- 5 • Susquehanna 1 and 2.⁶ (IR OCC-119, AG-020, AG-021)

6 In addition, Mr. McWhinney notes that three Canadian plants are potentially
7 for sale. Ontario Hydro is discussing the sale of the eight units at Bruce (of
8 which four are currently operating), and the AmerGen partners have formed
9 CanaGen to pursue these and possibly the twelve additional units at Ontario
10 Hydro's two other plants.

11 Thus, depending on which units one counts, near-term sale of Millstone
12 and Seabrook would compete in a market with fifteen to as much as thirty-
13 five other units (depending on whether Quad Cities and Susquehanna are
14 really on the block, and how many Ontario Hydro units are to be offered in
15 the near term).

16 He also expresses the opinion that a nuclear utility is likely to sell its
17 nuclear units as the electric industry in its state is restructured, if it owns less
18 than three units (or less than four units as part of a consortium, presumably to
19 include Palo Verde in the near-term "sell" category).

20 I have applied his criteria to the nuclear units that would be left after the
21 set listed above, excluding those owned by identified nuclear buyers

⁵Mr. McWhinney may be referring to plans of the minority owner to sell, but the sale of all of San Onofre would be consistent with his criteria.

⁶His identification of Quad Cities and Susquehanna as being "expected to sell" probably refers to the plant operators buying out the minority shares. Mr. McWhinney's confusion of plants with units (which he points out in IR AG-021) and his confusion of the sale of units with the sale of minority shares of units to joint owners, make his conclusory statements unreliable.

1 (Constellation, the Midwest Operating Company). There are eight such units
2 located in states (Texas and Michigan) that have already initiated
3 restructuring:

- 4 • Palisades
- 5 • Fermi 2
- 6 • South Texas Project 1, 2
- 7 • Cook 1, 2
- 8 • Commanche Peak 1, 2

9 It is not clear why, if these units are not on the market in the short term,
10 they would be in the longer term.

11 Another six units are in states that have not yet initiated restructuring:⁷

- 12 • Callaway
- 13 • Wolf Creek
- 14 • Summer,
- 15 • Washington Nuclear 2,
- 16 • Cooper, and
- 17 • Ft. Calhoun.

18 It is not clear that all the relevant states will restructure their industries. The
19 last three units on this list, which are publicly owned, may not be offered for
20 sale, even if their states restructure.⁸

21 In any case, applying Mr. McWhinney's criteria would result in
22 somewhere between six and fourteen units becoming available beyond the

⁷I do not include Florida Power's Crystal River unit, since Florida Power is in the process of merging with Carolina Power and Light, which already owns four units.

⁸The capital investment of a nuclear plant is much less expensive to carry under public ownership than private ownership.

1 near term, some of which might be offered for sale in 2002, at the same time
2 as a delayed Millstone sale. In any case, this is much less than the fifteen to
3 thirty-five units available in the near term.

4 **Q: Does Mr. McWhinney demonstrate that his projections are correct?**

5 A: No. Mr. McWhinney has no evidence to support his projections of which
6 units will come on the market, or when they will come on, or what types of
7 utilities will choose to retain their nuclear units. (See, e.g., IR AG-02: “I am
8 unaware of any evidence that these plants will be sold in the near term.”)
9 Some of his detailed judgements (e.g., that Central Hudson may be interested
10 in acquiring nuclear plants) seem unlikely to be correct. In other cases, Mr.
11 McWhinney’s vagueness (e.g., the confusions about plants and units,
12 minority shares and entire plants; or the lack of specificity about the timing
13 of the “near” term) makes his testimony difficult to understand.

14 If Mr. McWhinney’s input data and assumptions are correct, they
15 demonstrate that delay in the sale is preferable. If his data and assumptions
16 are incorrect, they contribute nothing to the record. Either way, CL&P has
17 presented no basis for concluding that the market for a near-term sale is
18 likely to be more favorable than the market for a sale in 2002 or 2003.

19 **IV. Plant-specific Considerations in the Timing of the Millstone Sale**

20 **Q: What plant-specific considerations affect the appropriate timing of the**
21 **Millstone auction?**

22 A: The considerations I have identified are:

- 23 • inclusion of other owners of Millstone 3,
- 24 • the opportunity for joint sale of Millstone and Seabrook,
- 25 • resolution of on-going litigation,

- 1 • the effects of continued Millstone operation on the sales price, and
2 • the distinction between shareholder and ratepayer benefits.
3 I discuss these issues in turn.

4 **A. *The Millstone 3 Joint Owners***

5 **Q: What issues regarding the inclusion of other joint owners of Millstone 3**
6 **in the auction should be of concern to the Commission?**

7 A: There are three such issues: the right of first refusal, the reduction in sales
8 price due to the nuisance value of minority owners, and the exclusion of
9 CMEEC (IR OCC-09).

10 **Q: What is the status of the other owners, with regard to participation in**
11 **the auction?**

12 A: Other than the NU subsidiaries and UI, New England Power (NEP) and
13 Montaup have reached agreements with NU on participating in the auction
14 and Vermont Electric Generation and Transmission Coop has proposed to
15 joint the auction (IR AG-002). CL&P claims to have no information on plans
16 of the eight other owners (IR AG-003), even though some of those joint
17 owners are negotiating with NU (IR OCC-16).

18 **Q: What is a right of first refusal?**

19 A: Associates in a business venture (including joint owners in power plants)
20 often agree that, should any participant decide to sell its share, each other
21 participant has the right to match any offer that the seller may accept from a
22 third party. Among other things, these provisions assure the participants in
23 the enterprise that they can choose to increase their share, rather than deal
24 with a new and perhaps undesirable associate.

25 **Q: Do the joint owners of Millstone 3 have a right of first refusal?**

1 A: Yes, as CL&P states in IR AG-004. Section 22 of the Sharing Agreement, as
2 amended in 1975, provides that the seller must provide notice to the
3 participants of “the proposed terms and conditions of the sale” at least eight
4 months prior to the proposed closing, and allows the other joint owners to the
5 exercise of the right of first refusal anytime within four months of the notice.⁹
6 (Bulk Attachment to IR OCC-012)

7 **Q: How many joint owners remain outside the auction agreement, and**
8 **potentially able to exercise the right of first refusal?**

9 A: I count eight such joint owners: three investor-owned utilities (CMP, CVPS,
10 and Fitchburg G&E) and five publicly-owned utilities (MMWEC, Chicopee,
11 CMEEC, Vermont G&T, and Lyndonville). CL&P purports to be “unaware
12 of the intent of any minority owner other than those who have indicated that
13 they intend to participate in the auction” (IR AG-003). This lack of interest is
14 worrisome.

15 **Q: What effect could the right of first refusal have on the Millstone auction?**

16 A: There are two potential effects. First, one or more potential bidders might
17 partner with a joint owner to utilize the right of first refusal. Such a potential
18 bidder could sit out the auction process, wait until the winning bidder is
19 selected, and then decide whether to purchase the plant at the terms of the
20 winning bid. Given the small number of potential bidders, the loss of one or
21 more from this auction process would likely reduce the ultimate price. Since
22 the right of first refusal does not require the joint owner to beat the winning

⁹The Millstone 3 right of first refusal applies to that unit specifically, and would not necessarily include Millstone 2. If the two units are sold as a package, as CL&P has proposed, the “the proposed terms and conditions of the sale” might include the simultaneous purchase of Millstone 2.

1 bid, just match it, and does not allow the winning bidder to offer a higher
2 price, the exercise of the right of first refusal does not increase the sale price
3 as would another bidder in the auction.

4 Second, the remaining potential bidders, aware of the right of first
5 refusal, are not likely to spend as much time and money in analyzing the
6 condition of Millstone and the economics of owning and operating the plant.
7 The prospect of having a favorable winning bid taken over by a joint owner
8 can hardly be attractive to a potential bidder. In the absence of such detailed
9 analysis, the bidders must be risk averse, and bid low, if they bother bidding
10 at all.

11 Mr. McWhinney puts the situation quite well:

12 A right of first refusal possessed by a third party could lower the value
13 of an asset to be sold in an auction. Prospective bidders may be less
14 likely to spend the necessary resources in preparing a bid for an asset
15 where there is a high likelihood that a third party will exercise this right.
16 Consequently, there could be fewer and less serious bidders and thus
17 theoretically a tendency for auction prices to be lower. (IR OCC-021)

18 **Q: Has the situation you have described actually occurred in the divestiture**
19 **of utility assets?**

20 A: Yes, twice. The first example occurred when FPL was selected by PG&E to
21 purchase some of its geothermal capacity, and the steam supplier (Calpine)
22 exercised its right of first refusal and acquired the plants at the price and
23 terms negotiated by FPL.

24 The second example, much closer to the Millstone sale situation, is that
25 of the sale of Nine Mile Point 1 and 41% of Nine Mile Point 2 by Niagara
26 Mohawk (NiMo) and New York State Electric and Gas (NYSEG). AmerGen
27 was selected as the winning bidder in June 1999. In December 1999,
28 Rochester Gas & Electric (RGE), a 14% owner of Nine Mile Point 2,

1 announced that it was assuming AmerGen's rights and responsibilities under
2 the agreements with NiMo and NYSEG. Since RGE owns only one other
3 nuclear unit, Ginna, it is not a good candidate to become a major nuclear
4 operator.¹⁰ Instead, Entergy will "lease, operate and maintain" Nine Mile
5 Point, "sell power to RGE at fixed cost," and assume responsibility for
6 "decommissioning the plants at a fixed price."¹¹ The result would be, in
7 RGE's view, to "transfer most of the plant operating risk to Entergy,
8 [provide] a golden opportunity to fund the retirement of our investment in
9 nuclear plants and provide a source of energy at a stable competitive price."
10 In all but name, then, Entergy has purchased Nine Mile Point at the price and
11 terms negotiated by AmerGen.¹² While AmerGen expressed a desire to
12 aggressively pursue the acquisition of Nine Mile Point, there was no
13 opportunity for it to offer a revised bid, and there has been no public
14 indication that AmerGen has found any mechanism to pursue the acquisition,
15 aggressively or otherwise. Entergy and RGE are better off than if Entergy
16 had participated vigorously in the auction, but AmerGen and the selling
17 utilities are worse off.

18 **Q: Would the right of first refusal a matter of concern to the sellers and**
19 **potential bidders in the Millstone sale?**

¹⁰The CEO of RGE admitted as much in an interview with Reuters on the day it exercised the right of first refusal: "the company's future is not in the nuclear generation business." ("INTERVIEW-RGS blocks AmerGen bid for N.Y. nuke," Reuters, December 22, 1999)

¹¹All quotes in this sentence and the next are from "RGS offers \$163 mln for Control of Two Nuclear Plants," Reuters, December 22, 1999.

¹²It appears that Entergy has also offered some inducement to RGE to participate in the transaction.

1 A: It certainly should be. UI reports that potential buyers of Seabrook “asked
2 about...the willingness of minority owners to sell their shares,” “want to buy
3 all minority shares,” and “questioned the contractual rights of joint owners”
4 (IR OCC-58). The right of first refusal is one of the “contractual rights of
5 joint owners” about which the buyers should be concerned.

6 **Q: How can the right of first refusal issue be resolved in a manner that**
7 **maximizes the market value of the Millstone sale?**

8 A: One approach would be to include all joint owners in the auction. Another
9 approach is to secure waivers of the right of first refusal from all joint owners
10 who are not participating in the auction. UI used a combination of these
11 approaches with respect to the New Haven Harbor sale (IR OCC-49).¹³

12 **Q: What has CL&P done to analyze the effect of rights of first refusal on**
13 **the sale price of power plants?**

14 A: So far as I can tell from discovery, nothing. It appears that CL&P has not
15 even bothered to find out which prior sales were associated with rights of
16 first refusal (or other rights), let alone understand how the sellers dealt with
17 those rights and how they affected the sales price. (IR OCC-036, OCC-045,
18 OCC-046, OCC-048.)

19 It is my understanding that NU has not requested waivers of joint
20 owners’ rights of first refusal, or to amend the Sharing Agreement to limit
21 those rights. Even the

22

23

¹³It is not clear whether all of these waivers were obtained prior to the auction of UI’s fossil assets. Those assets sold for considerably less than comparable plants in New England, perhaps due to the rights of first refusal.

1 **Q: Other than the right of first refusal, what other problems can be caused**
2 **by joint owners?**

3 A: The buyer may be reluctant to deal with minority owners, due to the nuisance
4 value of responding to the requests of those owners, concerns about potential
5 litigation over plant operation and maintenance (including the timing of
6 maintenance outage periods), and reluctance to share sensitive cost and
7 operating information (such as that in IR OCC-013) with third parties.

8 **Q: How much effect would the existence of minority owners have on the sale**
9 **price of Millstone, even after the right of first refusal is taken into**
10 **account?**

11 A: Those effects depend on the number of joint owners who join in the sale, and
12 are best estimated by extrapolation from past experience. Unfortunately, the
13 pricing of the nuclear sales tends to be complex and is not always fully
14 public.¹⁴

15 We do have one example in which a buyer explicitly offered a higher
16 price as its ownership level increased, even above the level required for
17 control of the plant. In the agreements to purchase the shares of the Colstrip
18 plants from Montana Power, PSE, and PGE, the buyer (PP&L) offered a
19 bonus to Montana Power if one of the smaller owners, or both, joined, and

¹⁴Mr. McWhinney's analyses of the sales prices are full of errors (e.g., discounting cash flows to utilities at 17.5%, ignoring contingent market-based sales), in addition to the usual information gaps. No reliance should be placed on his reconstructed sales prices.

In addition, the president of Dominion Generation describes the units that have sold to date as "in most cases, smaller, less cost-effective" and indicates that future units will sell for higher prices (IR OCC-108). So the sales prices of the units in Exhibit RTM-3, even if properly computed, would be of limited relevance to projecting the sales price of Millstone. Even the July 1999 presentation to the NU Board of Directors indicates that Millstone's value may be much greater than those achieved in earlier nuclear sales (see IR OCC-080).

1 offered a bonus to each of the smaller owners if the other joined the sale.
2 Even though PP&L already had a majority ownership share in the plant
3 (100% of units 1 and 2, and 55% of units 3 and 4) with just Montana Power
4 and PSE signed on, it offered them 5% more for their shares if PGE sold its
5 share as well.

6 The effect is likely to be more pronounced for nuclear units than for the
7 Colstrip coal unit. The sale price of a nuclear unit must represent the value of
8 the plant as an operating asset and the liability in the event of premature or
9 expensive decommissioning. An experienced nuclear owner is apt to expect
10 that elimination of minor owners will increase the value of the plant as an
11 operating asset, and perhaps also reduce the probability of premature
12 decommissioning. As a result, the proportionate effect on the net sales price
13 would be higher for nuclear than for fossil plants.

14 A 10% increase in the value per kilowatt for the elimination of minority
15 owners at Millstone would be worth tens of millions of dollars to CL&P and
16 UI.¹⁵

17 **Q: Other than the general problems of exclusion of minority owners, why**
18 **should the Commission be concerned with the exclusion of CMEEC**
19 **from the auction?**

¹⁵For example, the July 1999 presentation to the NU Board of Directors indicates that Millstone 2 would be worth \$..... million and Millstone 3 worth \$..... million with the NU Ramp performance (NU's projection of achievable, gradual improvement under its ownership), even with a% discount rate (which the Department has). (See IR OCC-080.) With those values, the CL&P and UI shares would be worth about \$..... million, before any discount for decommissioning risk, and a 10% decrease in value due to the problems raised by minority owners would amount to over \$.... million.

1 A: CMEEC has not yet been included in the auction (IR OCC-009). If CMEEC
2 sells its share after the majority ownership has already been sold, it is likely
3 to receive much less than it would have as part of the majority sale. The
4 Commission should make every effort to ensure that CMEEC is included in
5 the sale, regardless of whether it has settled with NU on the Millstone
6 prudence issue.

7 As CL&P acknowledges “participation [in the auction] by UI will likely
8 increase benefits for UI customers” (IR OCC-130). The same is equally true
9 for CMEEC customers. While CL&P is correct that CMEEC’s “share will
10 remain unaffected by the auction” (IR OCC-009), the value of its share will
11 be adversely affected by its exclusion.

12 ***B. Millstone and Seabrook***

13 **Q: What is the connection between the sale of Millstone and the sale of**
14 **Seabrook?**

15 A: The most important connection is the similarity in the design of Millstone 3
16 and Seabrook. As discussed in greater detail by OCC Witness Schlissel, joint
17 ownership of two similar units relatively close together should decrease the
18 costs of operating both of them.¹⁶

19 **Q: What effect would offering Millstone and Seabrook jointly have on the**
20 **price of Millstone?**

¹⁶As noted by the president of Dominion Generation, “in most cases, the economies of scale of [owning] additional units have a relatively small effect on the overall valuation because distance and station differences reduce the potential gains” (IR OCC-108-Bulk). Seabrook and Millstone 3 appear to be an exception to this rule, due to the similarity of the units and their proximity.

1 A: That approach would allow the Millstone price to capture some of the extra
2 value from the efficiencies of joint ownership. In addition, offering these
3 three units as a group would increase the likelihood that a new entrant to the
4 Northeast nuclear market (that is, some entity other than AmerGen and
5 Entergy) would be able to offer a competitive bid, further increasing the
6 likely sales price.

7 Of course, if separate bidders offer more for Seabrook and Millstone
8 separately than the highest bid for the plants together, the owners could still
9 sell the plants separately.

10 **Q: Would offering Millstone and Seabrook jointly present any serious**
11 **timing problems?**

12 A: It does not appear so. CL&P projects that the sale of Seabrook could be
13 approved in time to offer both units jointly on its current schedule for
14 Millstone (IR OCC-091). As I explain in this testimony, that schedule should
15 be delayed for other reasons, so even if the Seabrook approvals move more
16 slowly, they should be in hand before the Millstone auction should start.

17 **C. *Ongoing Litigation***

18 **Q: What is the potential effect on the Millstone auction of the appeal of the**
19 **stranded-cost cases (Dockets No. 99-02-05 and 99-03-04) by the OCC?**

20 A: While difficult to quantify, ongoing litigation is rarely a source of comfort to
21 bidders. Specifically, the appeal on the issue of the minimum bid may raise
22 concerns for some potential bidders. For example, if the minimum bid is
23 remanded to the Commission during the auction process, the schedule for the
24 auction might be extended. Similarly, a winning bidder would face the
25 prospect of the sale being delayed, or even of the auction being reopened, as

1 a result of a remand. This might even occur if the bid clearly (or arguably,
2 depending on its complexity) exceeded the new minimum bid.

3 Since there is no urgency in the sale (other than CL&P's desire to
4 maximize the value of the ConEd merger to NU's shareholders), the best
5 approach would be to get the appeals resolved, at least with respect to the
6 minimum bid, prior to the start of the auction.

7 ***D. Millstone operating risks***

8 **Q: How should the risk of operating Millstone affect the timing of the sale?**

9 A: The most important consideration is that another year or two of normal
10 performance will help demonstrate to potential buyers the condition of the
11 operating Millstone units, and help erase the stigma of the extended outage.
12 That consideration argues for delay in the sale.

13 Mr. McWhinney suggests that operating Millstone, even for another
14 year or two, would expose ratepayers to additional risks (direct, p. 13).
15 CL&P has not demonstrated any significant risk from operating Millstone in
16 this period, and (other than this remark by Mr. McWhinney) does not appear
17 to have addressed this issue on the record. Two of the three risks listed by
18 Mr. McWhinney ("changes in NRC requirements" and "changes in the spent-
19 fuel situation") could either increase or decrease the costs of operating and
20 decommissioning Millstone, and may thus increase or decrease the sales
21 price.

22 ***E. Shareholder Incentive and Ratepayer Benefits***

23 **Q: Are CL&P's incentives with regard to the auction well aligned with the**
24 **interests of ratepayers?**

1 A: No. ConEd has offered a \$1/share bonus to NU shareholders if a definitive
2 agreement to sell CL&P and WMECo's interests in Millstone 2 and
3 Millstone 3 is entered into and is recommended by the Utility Operations and
4 Management Unit prior to December 31 2000. That amounts to a \$137
5 million benefit to those shareholders, including NU officers (IR OCC-133).

6 In addition, an early sale may force joint owners to settle with NU in
7 their lawsuits over mismanagement of Millstone, rather than face the risk of
8 being left with a minority share of greatly diminished value.¹⁷

9 **Q: Do either of these considerations provide any benefit to CL&P or UI**
10 **ratepayers?**

11 A: No. An early sale benefits NU and possibly ConEd shareholders, but not
12 ratepayers.

13 **Q: What is the implication of these considerations?**

14 A: One important implication is that the Commission should not assume that
15 CL&P's positions in this case are motivated by reduction of costs to
16 ratepayers. CL&P's testimony should be treated with the same level of
17 skepticism the Commission would apply to testimony on such subjects as
18 cost of capital, where shareholder and ratepayer interests are clearly not in
19 alignment.

20 **Q: Does this conclude your testimony?**

21 A: Yes.

¹⁷Both UI and CL&P agree that the value of minority shares is impaired (IR OCC-130, OCC-053). This is also demonstrated by the very low price Montaup received for its share of Wyman 4 (about \$150/kW), when CMP's majority share of Wyman 4, and other contemporaneous New England oil and gas units, sold for at least \$400/kW. The implied minority-ownership discount is over 60%.