

October 14, 2011

UNITED STATES OF AMERICA
NUCLEAR REGULATORY COMMISSION

BEFORE THE ATOMIC SAFETY AND LICENSING BOARD

In the Matter of)	
)	
HONEYWELL INTERNATIONAL INC.)	Docket No. 40-3392
)	
(Metropolis Works Uranium)	ASLBP No. 11-910-01-MLA-BD01
Conversion Facility))	

NRC STAFF'S TESTIMONY REGARDING
HONEYWELL'S 2009 EXEMPTION REQUEST

Q.1. Please state your name, position and employer, and briefly describe your job duties. Also please identify any education, training, or prior work experience relevant to your job duties.

A.1.a. Roman Przygodzki. I am a Financial Assurance Project Manager in the NRC's Office of Federal and State Materials and Environmental Management Programs (FSME). As part of my job duties, I review and analyze decommissioning funding plans, cost estimates, financial instruments, contract language, financial statements (e.g., filings with the U.S. Securities and Exchange Commission), and other documents relevant to the Staff's review of various licensing actions. A statement of my professional qualifications is included as Exhibit NRC000002.

A.1.b. Kenneth Kline. I am also a Financial Assurance Project Manager in FSME. My job duties are similar to those of Roman Przygodzki. A statement of my professional qualifications is included as Exhibit NRC000003.

A.1.c. Thomas Fredrichs. I am a Senior Licensee Financial Policy Advisor in the NRC's Office of Nuclear Reactor Regulation (NRR). I serve as a Commission staff expert on the evaluation of reactor licensee financial qualifications and policies associated with electric industry restructuring and deregulation. I provide guidance, assistance, and recommendations to NRR management, other NRC Offices, and Commissioners and their staffs for all issues relevant to

licensee financial qualifications and performance; financial, economic, and insurance principles; corporate finance; financial markets; and the NRC mission. A statement of my professional qualifications is included as Exhibit NRC000004.

Q.2. On April 25, 2011, the NRC Staff denied Honeywell's application for an exemption from the financial assurance requirements at § 40.36(e). The exemption, if granted, would have excused Honeywell from meeting these requirements for the period May 2009 through May 2010. Could you provide the procedural background to the Staff's decision?

A.2. (R. Przygodzki, K. Kline) Honeywell applied for an exemption in April 2009. Exh. HNY000006. In September 2009, the Staff asked Honeywell to submit additional information to support its exemption request. Exh. NRC000010. Honeywell provided additional information in October 2009. Exh. HNY000008. After reviewing Honeywell's submissions, the Staff found that an exemption could not be granted. In December 2009, the Staff denied Honeywell's exemption request. Exh. HNY000011.

Honeywell thereafter appealed the denial decision to the D.C. Circuit for the District of Columbia. In December 2010, the Court vacated the decision and remanded Honeywell's exemption request to the NRC for further proceedings. *Honeywell v. NRC*, 628 F.3d 568 (D.C. Cir. 2010). The Court found that, although the NRC might have reasonably concluded that certain factors warranted denying Honeywell's exemption request, the NRC had not sufficiently explained the basis for its decision. *Id.* at 580–81.

Upon remand, the Staff reconsidered its December 2009 denial decision. The Staff did so by carefully reviewing the information available at the time of that decision. However, the Staff again found that Honeywell's exemption request must be denied. The Staff informed Honeywell of its decision by letter dated April 25, 2011. Exh. HNY000012.

Q.3. Had Honeywell previously requested a similar exemption?

A.3. (R. Przygodzki, K. Kline, T. Fredrichs) Yes. In December 2006, Honeywell requested an exemption from the requirements of § 40.36(e). Exh. HNY000004. In May 2007, the Staff

granted Honeywell a one-year exemption from those requirements. Exhs. HNY000009 and NRC000007. In 2008, Honeywell asked to extend its exemption for a year, and the Staff granted that request. Exhs. HNY000005, HNY000010 and NRC000008.

Q.4. What role did you have in reviewing Honeywell's exemption requests?

A.4.a. (T. Fredrichs) I was the primary financial reviewer for the first exemption request.

A.4.b. (K. Kline) I was the primary reviewer for the second exemption request. I also started reviewing the third exemption request soon after it was submitted in April 2009. Later that year I became busy with a variety of other projects, and Roman Przygodzki was brought in to assist with the review.

A.4.c. (R. Przygodzki) After approximately October 2009, I was the primary contributor to the Staff's decision on the third exemption request. I contributed to both the Staff's December 2009 initial decision on Honeywell's exemption request and the Staff's April 2011 reconsideration decision.

Q.5. What exactly did Honeywell ask for in its exemption requests?

A.5. (R. Przygodzki, K. Kline, T. Fredrichs) Honeywell asked for an exemption that would allow it to include goodwill in the definition of "tangible net worth" for purposes of meeting the first part of the financial test in 10 CFR Part 30, Appendix C. The Appendix C financial test allows qualified licensees to provide financial assurance through a self-guarantee, rather than by obtaining a surety bond or other financial instrument. Although the regulations in Part 30 do not apply directly to a source material licensee like Honeywell, § 40.36 incorporates the financial tests in Appendices A, C, D and E of Part 30.

Q.6. What does the Appendix C financial test require?

A.6. (R. Przygodzki, K. Kline, T. Fredrichs) The Appendix C financial test has three parts. First, the licensee's tangible net worth must be at least 10 times the total decommissioning cost estimate for all its facilities covered by a self-guarantee or parent company guarantee. This estimate includes costs related to facilities covered by a guarantee under the regulations of

another agency, such as the U.S. Environmental Protection Agency (EPA). We can refer to this first part of the Appendix C financial test as the “10-to-1 test.”

Second, the licensee must have assets in the United States that are at least 90 percent of its total assets or at least 10 times the total current decommissioning cost estimate for all its facilities covered by a guarantee. This second requirement could also be viewed as including a 10-to-1 test, but it is not a test from which Honeywell sought an exemption. So to be clear, when we refer to the “10-to-1 test,” we are referring to the first part of the Appendix C financial test, not the second.

Third, to meet the Appendix C financial test the licensee must have a current rating for its most recent bond issuance of AAA, AA or A as issued by Standard and Poor’s or Aaa, Aa, or A as issued by Moody’s.

Q.7. Honeywell appears to state that it is seeking an exemption only from certain provisions in § 40.36(e) and Appendix C, namely the 10-to-1 requirement in the first part of the Appendix C financial test. Is that correct?

A.7. (R. Przygodzki, K. Kline, T. Fredrichs) It is more accurate to say that Honeywell is seeking an exemption from the requirements of § 40.36(e) generally, and that it is proposing a variant of the Appendix C financial test as a compensatory measure. Honeywell does not need an exemption from Appendix C itself, because it does not have to comply with Appendix C. The self-guarantee method in Appendix C is only one of many ways to provide financial assurance. If Honeywell wants to provide financial assurance through one of the other methods in § 40.36(e), it does not need an exemption to do so. However, if Honeywell seeks to use a method not described in § 40.36(e)—which is in fact what it is seeking—it needs an exemption.

Q.8. Why is this important to clarify?

A.8. (R. Przygodzki, K. Kline, T. Fredrichs) First, because we should be precise about the type of exemption Honeywell is seeking and the effect of granting or denying its exemption request. Second, because Honeywell’s framing of its exemption request overlooks the fact that

there are numerous other ways for a licensee to provide financial assurance. For example, under the regulations in effect in 2009, Honeywell could have provided financial assurance through prepayment, a surety method, insurance, or an external sinking fund coupled with a surety method or insurance. Further, Honeywell's surety method or external sinking fund could have been established through a variety of different instruments.

Q.9. When the Staff granted exemptions for 2007 and 2008, didn't its decisions state that Honeywell was being exempted from the requirements of Appendix C?

A.9. (R. Przygodzki, K. Kline, T. Fredrichs) While those decisions referred to Appendix C, the effect of those decisions was to allow Honeywell to provide financial assurance in a manner that was not permitted under § 40.36(e). For that reason, it would have been more precise to say that Honeywell's exemptions were from § 40.36(e) generally, rather than from Appendix C specifically.

Q.10. Before addressing the particulars of Honeywell's exemption requests, we'll ask you to explain some of the terms used in the Appendix C financial test. First, what is tangible net worth?

A.10. (R. Przygodzki, K. Kline, T. Fredrichs) Tangible net worth is stockholders' equity less intangible assets and less goodwill.

Q.11. What are intangible assets?

A.11. (R. Przygodzki, K. Kline, T. Fredrichs) Statement of Financial Accounting Standards (SFAS) 141R defines an intangible asset as an "asset (not including a financial asset) that lacks physical substance." Exh. HNY000035 at 3. SFAS 141R also provides examples of intangible assets. These include patents, trademarks, customer lists, and licensing or royalty agreements. Exh. HNY000035 at 41–48.

Q.12. What is goodwill?

A.12. (R. Przygodzki, K. Kline, T. Fredrichs) SFAS 141R defines goodwill as "an asset [that] represent[s] the future economic benefits arising from other assets acquired in a business

combination that are not individually identified and separately recognized.” Exh. HNY000035 at 2.

Q.13. The issue now before the Atomic Safety and Licensing Board is whether Honeywell can prove it should be granted an exemption from § 40.36(e) for the period May 2009 through May 2010. However, Honeywell has previously claimed that its 2009 exemption request was nearly identical to the prior exemption requests that the Staff granted. It may therefore help to summarize why the Staff granted the first two exemption requests. Could you address Honeywell’s December 1, 2006 (first) exemption request, which the Staff granted on May 11, 2007?

A.13. (T. Fredrichs) The Staff granted Honeywell an exemption in 2007 based on the company’s bond ratings and the specific financial data Honeywell submitted in connection with its request. To support its exemption request, Honeywell relied on its end-of-year financial data from 2005, as adjusted to reflect data from the first quarter of 2006. At that time Honeywell’s ratio of tangible net worth to decommissioning costs was 7.9-to-1. Although this ratio was slightly lower than the 10-to-1 ratio required by the self-guarantee test in Appendix C of Part 30, it was actually higher than the 6-to-1 ratio incorporated in parent-company-guarantee test in Appendix A of Part 30. With goodwill included, Honeywell’s ratio of tangible net worth to decommissioning costs was 39.5-to-1. Exhs. NRC000018, NRC000020 and HNY000009 at 53.

Although the Staff granted Honeywell an exemption for 2007, we also told Honeywell that if it sought to permanently use goodwill to meet the 10-to-1 test, it would have to seek a change through rulemaking. Because the NRC was then revising its decommissioning planning rules, and because the financial assurance requirements in those rules were also subject to revision, Honeywell had an opportunity to present its arguments on this point. In order to limit any risk associated with granting the 2007 exemption, and also to monitor the progress of the ongoing rulemaking, we added a license condition limiting Honeywell’s exemption to one year. As explained in the Technical Evaluation Report accompanying Honeywell’s license renewal,

part of the reason we added this condition was so that we could reassess Honeywell's exemption after we evaluated any comments submitted on the proposed decommissioning planning rule. Exh. HNY000009 at 53–54.

Q.14. What about Honeywell's April 11, 2008 (second) exemption request, which the Staff granted on August 22, 2008?

A.14. (K. Kline) Granting an exemption in 2008 was a much closer call. To support its exemption request, Honeywell relied on end-of-year financial data from 2007. However, Honeywell's tangible net worth had declined significantly from when we granted the first exemption, and by the end of 2007 Honeywell actually had negative tangible net worth. Exhs. NRC000018, NRC000020 and HNY000007 at 2.

At the same time, several factors weighed in favor of the exemption. Honeywell continued to maintain the same bond ratings it had in previous years, and we did not yet have strong reason to question the reliability of bond ratings. 2007 was also the first year that Honeywell had negative tangible net worth, and its history suggested that it would come back into compliance with the 10-to-1 test. Further, although the economy had experienced difficulties over the previous year, there were some positive signs. In July 2008 the Federal Reserve issued a Monetary Policy Report suggesting that the economy was stabilizing, or the economic downturn at least slowing. Exh. NRC000024. The report stated that policy actions taken by the Federal Reserve had produced some positive effects, and it projected that economic growth would "pick up gradually" over the next two years. *Id.* at 2. Although the report was not entirely optimistic, it nonetheless stands in contrast to the highly unfavorable economic reports from late 2008 and 2009.

Q.15. Now let's focus on the third exemption request. What information did the Staff consider in reaching its December 11, 2009 denial decision?

A.15. (R. Przygodzki, K. Kline) We based our decision on Honeywell's application in April 2009 and the supplemental information Honeywell provided in October 2009. Exhs.

HNY000006 and HNY000008. In terms of the financial data we considered, in its 2009 request Honeywell relied on end-of-year financial data from 2008. During our review we also considered general financial and economic information available up to the date of our decision.

Q.16. Why did the Staff deny Honeywell's 2009 exemption request?

A.16. (R. Przygodzki, K. Kline) We had numerous reasons for denying the 2009 request, not all of which were included in our December 2009 decision. In that decision, we focused on Honeywell's multi-billion-dollar decline in tangible net worth between the end of 2007 and the end of 2008. We also responded to Honeywell's claim that its 2009 request was consistent with the proposed decommissioning planning rule that the NRC issued in January 2008.

Q.17. Honeywell's hearing request challenges the Staff's April 2011 reconsideration decision, so we'll focus on that decision. First, could you explain the format of the April 2011 decision?

A.17. (R. Przygodzki) The format tracks the arguments Honeywell made in support of its 2009 exemption request. In particular, the Staff addresses the arguments Honeywell made in the October 2009 supplement to its exemption request.

Q.18. What information did you consider in reaching the April 2011 reconsideration decision?

A.18. (R. Przygodzki) Because we were reconsidering whether we made the correct decision when we denied Honeywell's exemption request in December 2009, we limited our review to information available as of December 11, 2009, the date of denial.

Q.19. Couldn't you have considered more recent information? For example, by April 2011 you could have reviewed Honeywell's end-of-year 2010 data, right?

A.19. (R. Przygodzki) We could have, but doing so would have removed any need for us to address Honeywell's arguments in favor of the 2009 exemption. We could have simply looked at the 2010 data and said, "O.k., you didn't default, fail to meet the other parts of the Appendix C financial test, or enter decommissioning last year; you can have an exemption." It would be a bit like negotiating an insurance premium after the period of coverage expires. Because the period has expired, you don't necessarily need to assess risk in the same manner. However, in

this case the D.C. Circuit found that the NRC's December 2009 denial decision raised issues that were capable of repetition. *Honeywell*, 628 F.3d at 576–78. So, we took another look at those issues and tried to decide whether in December 2009 we made the right decision, in which case we needed to explain our decision better, or whether it was the wrong decision, in which case we should retroactively grant Honeywell an exemption for 2009.

Q.20. The broader issue raised by the D.C. Circuit's remand order is whether in 2009 there were any changes of circumstances that distinguished Honeywell's 2009 exemption request from its 2006 (first) and 2008 (second) requests, which the Staff granted. How did the Staff address that issue in its April 2011 decision?

A.20. (R. Przygodzki) Honeywell's arguments in support of its 2009 exemption request were essentially the same as in prior years. In the sections of our April 2011 decision addressing Honeywell's arguments, we explain why arguments that might have been persuasive in 2007 or 2008 were no longer persuasive in 2009. In other words, we distinguish our 2007 and 2008 decisions by pointing to specific changes in the factors Honeywell relied upon in support of each exemption request. We also point to broader changes in the economy between the 2008 and 2009 requests that were relevant to reviewing Honeywell's latter request.

Q.21. The first factor you address in the April 2011 decision is bond ratings. Could you explain how you addressed Honeywell's arguments on this issue?

A.21. (R. Przygodzki) Honeywell's bond ratings were a key basis for its 2006 and 2008 exemption requests and for the Staff's approval of those requests. By 2009, however, the global financial crisis forced us to take a different view of bond ratings.

Q.22. Could you explain what you mean by "global financial crisis"?

A.22. (R. Przygodzki) I'm referring to the sharp downturn in the global economy that began in 2007 and accelerated in late 2008.

Q.23. Does "crisis" accurately describe this economic downturn?

A.23. (R. Przygodzki) “Crisis” is how the United States government itself has described the economic changes of the past few years. In fact, the federal government created a Financial Crisis Inquiry Commission to “examine the causes of the current financial and economic crisis in the United States.” Exh. NRC000047 at *xi*. The Federal Reserve has also prepared a document titled, “The Financial Crisis: A Timeline of Events and Policy Actions.” Exh. NRC000048. In brief, “financial crisis” accurately describes the events of the past few years.

Q.24. Can you give some examples of how businesses were affected by the financial crisis?

A.24. (R. Przygodzki) The two entities I just mentioned, the Financial Crisis Inquiry Commission and the Federal Reserve, have issued reports or timelines summarizing significant events in the crisis. Exhs. NRC000047 and NRC000048. To the extent these documents address events up to December 11, 2009, the date we initially denied Honeywell’s 2009 exemption request, they provide useful summaries of certain information we considered in reaching our initial and reconsideration decisions. In particular, I’d refer to pages 6 through 35 of the Federal Reserve timeline. Exh. NRC000048 at 6–35.

In terms of contemporaneous reports from late 2008 and through 2009, there were numerous examples of large corporations in severe financial distress. A number of significant events took place in September 2008. That month the federal government seized Fannie Mae and Freddie Mac, assuming more than \$5 trillion in liability. Exh. NRC000027 at 1, 4. Lehman Brothers filed for bankruptcy, which was the largest bankruptcy filing in United States history. Exhs. NRC000025, NRC000026 and HNY000024 at 3. Federal regulators seized Washington Mutual, making the company the largest savings and loan failure ever. Exhs. NRC000029 and NRC000047 at 365. Citigroup agreed to purchase (and Wells Fargo eventually purchased) Wachovia, a transaction that narrowly averted the failure of the latter company. Exhs. NRC000031, NRC000032 and NRC000048 at 9. On September 18, 2008, the Wall Street Journal warned that the financial crisis had entered a “new, far more serious phase.” Exh. NRC000028 at 1. That was in an article titled, “Worst Crisis Since ‘30s, With No End Yet in

Sight.” Then, in October 2008, the federal government took a number of steps that reflected the severity of the financial crisis. This included passing the Emergency Economic Stabilization Act of 2008, commonly referred to as the “bailout package,” which included the \$700 billion Troubled Asset Relief Program (TARP). Exhs. NRC000034 at 3 and NRC000047 at 371–72.

The financial crisis continued throughout 2009. In January 2009, the Congressional Budget Office stated that “[t]he sudden decline in economic activity in the second half of [2008] signaled that the recession could be severe . . . [n]ormally, sharp contractions in economic activity are followed by rapid rebounds, but this forecast anticipates that the recovery in 2010 will be slow[.]” Exh. NRC000037 at 4. In May 2009, U.S. corporate defaults for the year had already matched the total defaults in all of 2008. Exh. NRC000039. In June 2009, Standard and Poor’s predicted that defaults in 2009 would increase 117% over defaults in 2008. Exh. NRC000041. In August 2009, the Federal Deposit Insurance Commission (FDIC) reported that FDIC-insured institutions lost \$3.7 billion in the second quarter of 2009. Exh. NRC000042. A Bain forecast issued in September 2009 predicted that corporate defaults would reach “unprecedented” levels that year. Exh. NRC000043. In November 2009, CIT Group filed for bankruptcy protection. Exh. NRC000045. This was significant because the federal government had previously purchased \$2.3 billion of CIT preferred stock in December 2008 under TARP, and CIT’s bankruptcy was expected to eliminate the equity stakes of all CIT’s current shareholders, including the government. Exhs. NRC000047 at 396 and NRC000048 at 34.

Q.25. How did the ongoing financial crisis affect the Staff’s view of bond ratings?

A.25. (R. Przygodzki) In brief, it caused us to question the weight we assigned bond ratings when assessing Honeywell’s ability to self-guarantee decommissioning funding. There were numerous reports in 2009 suggesting that credit rating agencies were slow to react to dire changes in companies’ financial positions. The World Bank article marked as Exhibit NRC000044 makes this point. Part of the problem was that credit rating agencies might not timely react to market events. In other words, even if a company’s finances showed a

downward trend, agencies might not capture this trend in their ratings until the company experienced significant financial difficulty. One example was Lehman Brothers, which Standards and Poor's did not downgrade until the same day the company filed for bankruptcy. Exh. NRC000026. The Staff was also concerned that credit rating agencies might be slow in downgrading the ratings of certain companies due to the adverse impact a downgrade might have on the company. This is also mentioned in the World Bank article. Exh. NRC000044 at 4–5. Other reports identified additional concerns with credit rating agencies, particularly with regard to conflicts of interest and information disclosure. Exh. NRC000046 at 2. In sum, the Staff was exceedingly reluctant to exempt Honeywell from the NRC's financial assurance rules at a time when the global economy was in crisis and there were significant concerns over the reliability of bond ratings.

Our concerns over the reliability of bond ratings were later reflected in the final decommissioning planning rule published in June 2011. Exh. NRC000015. The final rule states, "Recent data suggests that regulators should not rely on a bond rating by itself to provide financial assurance, as discussed in paragraph N.7 of this section." *Id.* at 13 (76 Fed. Reg. at 35,524). The rule also states, "The data suggests that a high bond rating by itself does not necessarily signal financial strength." *Id.* at 14 (76 Fed. Reg. at 35,525). These were the same concerns the Staff had when we were reviewing Honeywell's 2009 exemption request. I would emphasize that we were not prospectively applying criteria in the final rule to Honeywell's exemption request. Rather, I'm simply noting that the information we considered in 2009 was later deemed important in the NRC's rulemaking.

Q.26. Hadn't the global financial crisis already arrived by the time the Staff granted the 2008 exemption?

A.26. (R. Przygodzki, K. Kline) To some extent. However, soon after the Staff granted Honeywell's 2008 exemption request, the economy experienced another sharp downward turn. Exh. NRC000038 at 5, 6, 17. The Staff granted the 2008 exemption request in August 2008.

As mentioned above, the very next month saw bankruptcies or federal intervention involving companies such as Lehman Brothers, Washington Mutual, Fannie Mae, Freddie Mac, and Wachovia. The federal government also took other emergency measures, such as a temporary guarantee program for money market funds and an increase in FDIC insurance coverage. Exhs. NRC000030 and NRC000033. In sum, it is accurate to say that, soon after the Staff granted Honeywell's 2008 exemption request, the financial crisis entered a "new, far more serious phase." Exh. NRC000028 at 1.

Q.27. Honeywell argued that the failing companies were primarily in the financial sector. Was that so?

A.27. (R. Przygodzki, K. Kline) No. According to Moody's, "non-financial corporate issuers were the main driver of default volumes in 2009 . . . non-financial companies accounted for 74.8% of volume in 2009, compared to 20.6% in 2008." Exh. HNY000025 at 3. Examples of non-financial defaults in 2009 included Ford, General Motors, Chrysler, Lyondell Chemical Company, XM Satellite Radio, and Level 3 Communications. *Id.* at 5, 18, 23.

Q.28. In its October 2009 supplement, Honeywell seems to suggest that, because it is a multi-industry conglomerate, it was resistant to changes in the economy. Did you consider that?

A.28. (R. Przygodzki, K. Kline) The financial crisis in 2009 affected broad sectors of the global economy. So, Honeywell's multi-industry operations did not seem to immunize the company from the impacts of the financial crisis. Further, Honeywell's share price in 2008 generally followed market trends, and in some cases was subject to more significant downward trends. Exh. NRC000019. This likewise gave the Staff reason to conclude that, for the period covered by the 2009 exemption request, Honeywell would not be immune from changes affecting the global economy. In its SEC filings, Honeywell itself acknowledged that "industry and economic conditions may adversely affect the market and operating conditions of [its] customers, which in turn can affect demand for [its] products and services and [its] results of operations." Exh. HNY000018 at 11. Honeywell added that its "consolidated operating results are [in part] driven

by [the] impact of global economic growth rates . . . and industry conditions on demand in [its] key end markets.” *Id.* at 25. Finally, a large part of Honeywell's revenue comes from its aerospace operations, and in 2009 Moody's reported that the aerospace industry was particularly sensitive to fluctuations in the global economy. NRC0000052 at 4.

Q.29. What general effect did the global financial crisis in 2009 have on the Staff's decision?

A.29. (R. Przygodzki, K. Kline) Given the high degree of economic uncertainty, we carefully reviewed the factors upon which we previously relied in granting Honeywell's exemption requests. We also had fresh in our memory the market downturn of September 2008, which occurred soon after we granted the 2008 exemption request. We did not want to be in a position where we granted Honeywell's request in December 2009, only to see Honeywell swept into a financial downturn in January 2010.

Q.30. Would you have granted Honeywell's 2009 exemption request had it not been for these broader economic concerns?

A.30. (R. Przygodzki) No. As we'll discuss below, there were also numerous other factors that caused us to deny the 2009 exemption request.

Q.31. The next part of the Staff's April 2011 denial letter addresses free cash flow. Why did you reject Honeywell's claim that its free cash flow supported granting an exemption?

A.31. (R. Przygodzki) First, free cash flow is just that—free. It is not committed to the NRC, and the NRC has no way of ensuring it will be available to fund decommissioning activities. For that reason the NRC's regulations do not allow licensees to use free cash flow as a means of financial assurance. Second, free cash flow may be subject to sudden fluctuations. If revenue goes down, free cash flow may go down. If a company goes out of business and ceases operations, free cash flow may drop substantially overnight. When deciding whether to grant Honeywell an exemption, one issue we considered is whether there would be sufficient assurance Honeywell could satisfy its decommissioning obligations in a time of financial distress. Because free cash flow is not committed to the NRC and financial distress might

substantially eliminate this potential source of funding, we did not find Honeywell's arguments regarding cash flow to be persuasive.

Q.32. Honeywell also stated that it had \$22.5 billion in assets at the end of 2008. Did you consider that?

A.32. (R. Przygodzki) Yes, but it did not support granting an exemption. The reason is that the financial test in Appendix C already considers the assets of the licensee. Specifically, the second part of the test requires that the licensee have assets in the United States amounting to at least 90 percent of total assets or at least 10 times its total cost estimate for all decommissioning activities for which the licensee is responsible. Had we granted Honeywell an exemption based on its assets, we would have been double counting one leg of the Appendix C financial test.

Q.33. The Staff's April 2011 denial letter next focuses on Honeywell's decline in tangible net worth prior to its 2009 exemption request. Why was that significant?

A.33. (R. Przygodzki) For several reasons. Honeywell's tangible net worth when it requested the 2009 exemption was negative \$5.3 billion. That was a decline of \$3.8 billion from when it submitted its 2008 exemption request. For 2009, Honeywell would therefore have needed to rely on significantly more goodwill to meet the 10-to-1 test in Appendix C. Whereas Honeywell needed \$3.7 billion in goodwill to meet the test in 2008, for 2009 that amount would have been \$6.8 billion. Exhs. NRC000018 and NRC000021.

Q.34. Why was that important?

A.34. (R. Przygodzki) Compared to tangible assets, and even compared to other intangible assets, goodwill is relatively illiquid. What this means is that a company may experience delays in converting goodwill into cash. Goodwill is relatively illiquid because it can't be separated from a business or business line. To quote from the GAAP (Generally Accepted Accounting Principles) Guide, "The rights to a patent, copyright, or franchise can be identified separately and bought or sold. Goodwill, on the other hand, is inseparable from a business and is

transferable only as an inseparable intangible asset of an enterprise.” Exh. NRC000023. In other words, a company like Honeywell would have to negotiate for the sale of an entire business or business line in order to convert goodwill into cash.

Q.35. Why is that a concern?

A.35. (R. Przygodzki) Because it could lead to delays in decommissioning. If Honeywell had to spend months or years negotiating the sale of a business or business line in order to obtain funds to begin decommissioning its facility, that could adversely affect public health and safety, as well as life and property.

Q.36. How is that so?

A.36. (R. Przygodzki) The NRC has found that “[i]nadequate or untimely consideration of decommissioning, specifically in the areas of planning and financial assurance, could result in significant adverse health, safety and environmental impacts.” Exh. NRC000012 at 2 (53 Fed. Reg. at 24,019). In particular, “[t]hese impacts could lead to increased occupational and public doses, increased amounts of radioactive waste to be disposed of, and an increase in the number of contaminated sites.” *Id.* Accordingly, even if Honeywell’s sale of a business or business line eventually generated funds sufficient to decommission its facility, the public could suffer as a result of the delay in decommissioning.

Q.37. Does that explain why the 10-to-1 test in Appendix C looks to tangible net worth, as opposed to net worth generally?

A.37. (R. Przygodzki, T. Fredrichs) Yes. The NRC adopted the tangible-net-worth component of the Appendix C test based in part on rulemaking by the EPA. The EPA adopted a tangible-net-worth requirement in its financial rules precisely because of concerns over whether intangible assets might be promptly available to pay for cleanup costs. Exh. NRC000011 at 4 (47 Fed. Reg. at 15,035). The EPA explained that assets of firms often include intangibles such as goodwill that may be difficult to convert into cash to pay for closure and post-closure costs.

Id. For that reason, the EPA included a \$10 million tangible net worth requirement in its financial test. *Id.*

This concern over the relative illiquidity of certain assets is heightened in the case of goodwill. Although a company might be able to sell a patent on its own, it won't be able to sell separately a portion of the goodwill associated with a business line. Exh. NRC000023. It should be noted that Honeywell never sought to use intangible assets such as patents or trademarks to meet the 10-to-1 test. Rather, it sought only to use goodwill.

Q.38. Wouldn't these questions surrounding goodwill have been a concern when the Staff granted the 2007 and 2008 exemptions?

A.38. (R. Przygodzki, K. Kline, T. Fredrichs) Yes, but not at the same level. When the Staff granted the 2007 exemption, Honeywell's ratio of tangible net worth to decommissioning liability was positive 7.9-to-1. Although Honeywell had negative tangible net worth when we granted the 2008 exemption, its ratio of tangible net worth to decommissioning liability was negative 6.5-to-1. For 2009, however, that ratio was negative 33.7-to-1. Exhs. NRC000018 and NRC000020. Honeywell's ratio therefore was not only declining, but the decline was accelerating. And as stated above, whereas Honeywell needed \$3.7 billion in goodwill to meet the 10-to-1 test in 2008, for 2009 it would have needed \$6.8 billion. Exhs. NRC000018 and NRC000021. This meant that Honeywell was greatly increasing its reliance on an asset class that might not promptly pay for decommissioning costs.

Q.39. Were there any other concerns about goodwill?

A.39. (R. Przygodzki) The Staff was concerned that Honeywell's goodwill might be subject to impairment during the period covered by the exemption. Impairment occurs when the implied fair value of goodwill is less than its carrying amount. HNY000033 at 12. When the Staff was reviewing Honeywell's 2009 exemption request, we were highly concerned by reports predicting that goodwill impairments would increase in the near future. In June 2009, for example, KPMG advised that "the period of goodwill impairments is far from over" and predicted that "the

situation could actually worsen still further during the remainder of 2009.” Exh. NRC000040. Further, at the end of 2008 the parent company of Western Nuclear, an NRC licensee that is covered by a parent company guarantee, took an almost \$6 billion loss due to impairment of goodwill. Exh. NRC000036 at 65.

The Staff recognizes that financial standards require goodwill to be tested for impairment at least annually, or whenever there might be a change of circumstances potentially affecting its value. Exh. HNY000033 at 14–15. However, given the significant economic uncertainty in late 2009, the Staff was concerned that such tests might not have captured a sudden change in the value of Honeywell’s goodwill. In addition, whether to test for goodwill impairment between annual tests may depend heavily on the judgment of company officials. Under SFAS-142, “Goodwill of a reporting unit shall be tested for impairment between annual tests if an event occurs or circumstances change that would more likely than not reduce the fair value of a reporting unit below its carrying amount.” *Id.* at 15. Determining when this threshold is met could in certain cases be quite difficult. The KPMG article mentioned above, titled “Goodwill Impairment in 2009,” explained that “valuation is not an exact science and that it has never been more difficult than it is now to ascribe a value to an entity[.]” Exh. NRC000040.

Q.40. Honeywell had approximately \$10 billion in goodwill at the time of its 2009 exemption request. Why this concern over impairment?

A.40. (R. Przygodzki) Because in 2009 Honeywell was not only seeking to use an unprecedented amount of goodwill to meet the 10-to-1 test; it was seeking to use an unprecedented percentage of its goodwill to meet the test. For 2007, Honeywell needed to use only 7% of its goodwill to meet the 10-to-1 test. By 2008 that had climbed to 40%. By 2009, however, Honeywell would have needed to use 67% of its goodwill to meet the test. Exhs. NRC000018 and NRC000022. This was a 67% increase from 2008, when Honeywell needed only 40% of its goodwill to meet the test, and an 857% increase from 2007, when it needed only 7% of its goodwill to meet the test. In other words, Honeywell was getting closer to the point

where even its goodwill would not allow it to meet the test. This increased the chance that, if Honeywell suffered significant goodwill impairment in 2009, it would fall below the 10-to-1 threshold.

In addition, if Honeywell were to fall into financial distress, it might have to sell off business lines in order to generate funds. In that case, Honeywell might realize much less from the sale of goodwill than its book value. As an example, when Tyco International divested Tyco Capital, it realized a goodwill impairment of well over \$6 billion, which comprised nearly all of the goodwill associated with Tyco Capital. Exh. NRC000051 at 94–95. Again, because in 2009 Honeywell would have needed to use such a high percentage of its goodwill to meet the 10-to-1 test, goodwill impairment was a significant concern.

Q.41. Was there anything else significant about Honeywell’s decline in tangible net worth between 2008 and 2009?

A.41. (R. Przygodzki, K. Kline, T. Fredrichs) Honeywell’s continuing decline in tangible net worth made clear that it would not soon return to compliance with § 40.36(e). When Honeywell initially requested an exemption, it suggested that its need for an exemption would be temporary. Honeywell explained that it had also failed to meet the 10-to-1 test in 2002, but that “by June 30, 2003, Honeywell had returned to full compliance with all three legs of the financial test for self-guarantee of decommissioning liability and remained in compliance until December 31, 2005.” Exh. NRC000006 at 1. Although in 2008 we might have seriously questioned whether Honeywell would soon return to compliance with the Appendix C financial test, by 2009 it was much more evident Honeywell would not. What might have been an anomaly was now a trend.

Q.42. Do we know why Honeywell’s tangible net worth continued to decline?

A.42. (R. Przygodzki) One contributing factor was Honeywell’s business strategy. In the October supplement to its 2009 exemption request, Honeywell explained that it is an acquisitive company, which results in an increase in goodwill but a corresponding decline in tangible net

worth. Exh. HNY000008 at 2, 5. This strategy had the effect of pushing Honeywell further out of compliance with the 10-to-1 test.

Q.43. The next part of the April 2011 denial letter states that an exemption for 2009 would not be in the public interest. Can you explain this finding?

A.43. (R. Przygodzki) The requirements for granting an exemption to a licensee like Honeywell are at 10 C.F.R. § 40.14. Among other requirements, Honeywell must show that its requested exemption is in the public interest. For reasons stated elsewhere in our letter, we found that granting an exemption in 2009 would have increased the risk that funds might not be readily available to begin decommissioning the Metropolis Works Facility. Notwithstanding Honeywell's arguments, we found there was great uncertainty over how it might be affected by the ongoing global financial crisis. We also had strong reasons to reexamine the weight we had previously given bond ratings when granting the 2007 and 2008 exemptions. Further, Honeywell's increased reliance on goodwill raised significant concerns that, if it fell into financial distress, there might be a delay in converting assets into decommissioning funds. In brief, we found that granting the 2009 exemption would not be sufficiently protective of public health and safety.

Q.44. Did you consider the financial burden on Honeywell if the Staff denied its exemption request?

A.44. (R. Przygodzki) We did consider Honeywell's arguments regarding its financial burden in complying with § 40.36(e). Honeywell estimated it would cost between \$1.5 and \$2 million a year to obtain a letter of credit for the Metropolis Works Facility. Exh. HNY000008 at 11. Honeywell's high-end estimate of \$2 million was still less than 1.5% of the \$156 million in decommissioning costs for which it needed to provide financial assurance. When the NRC adopted the self-guarantee rule in 1993, this percentage, 1.5%, was the percentage that the NRC assumed licensees would typically need to pay for a surety bond or other form of financial assurance. Exh. NRC000013 at 1 (58 Fed. Reg. at 68,726). Honeywell's estimated cost of

complying with § 40.36(e) therefore could not be considered unreasonably high. Further, this cost was less than one one-thousandth (approximately 0.09%) of Honeywell's annual free cash flow.

Honeywell's burden in obtaining a letter of credit was also not unique. The NRC has not exempted any other licensee from the requirements of the self-guarantee or parent company guarantee tests in Appendices A and C to Part 30. In other words, if a licensee cannot meet those tests, it has to pay for a financial instrument to cover decommissioning costs. Likewise, in 2009 Honeywell itself did not use a self-guarantee or parent company guarantee to cover its decommissioning costs under any other program. Honeywell reported \$946 million in environmental liabilities at the end of 2008. Exh. HNY000018 at 84–85. Apart from its liabilities associated with the Metropolis Works Facility, none of Honeywell's liabilities were covered by a guarantee. If Honeywell had used a guarantee for other liabilities, the guarantee would have appeared on Honeywell's financial test submission to the NRC, and Honeywell would have been required to include the covered costs when determining whether it met the Appendix C financial test.

Q.45. But weren't the costs to Honeywell in 2009 similar to the costs when the Staff granted the 2007 and 2008 exemptions?

A.45. (R. Przygodzki, K. Kline, T. Fredrichs) Honeywell's estimated costs for obtaining a financial instrument in 2007 and 2008 were somewhat less. Regardless, the Staff did not grant exemptions for those years based solely on a finding that Honeywell would incur certain costs in complying with § 40.36(e). Rather, the Staff found that those costs were unnecessary in light of current economic conditions and the specific financial data Honeywell submitted with its requests. Those parts of the calculation had changed by 2009, and Honeywell's requested exemption could no longer be considered in the public interest.

Q.46. The April 2011 denial letter does not specifically mention the other requirements for granting an exemption that are stated in § 40.14. Regarding the first requirement in § 40.14, was Honeywell's exemption authorized by law?

A.46. (R. Przygodzki) My understanding is that an exemption is "authorized by law" as long as it is not prohibited by law. So, the exemption would meet that requirement.

Q.47. What about the second part of § 40.14, which requires that the exemption not endanger life or property or the common defense and security?

A.47. (R. Przygodzki) Granting Honeywell's 2009 exemption request could, in fact, have endangered life and property. Granting the 2009 exemption would have allowed Honeywell to rely on a self-guarantee that was not as strong as that contemplated by Appendix C. This would have increased the risk that funds might not be readily available to decommission the Metropolis Works Facility. Further, the statements of consideration underlying the NRC's financial assurance rules make clear that delays in decommissioning can endanger life and property. For example, a delay could "lead to increased occupational and public doses, increased amounts of radioactive waste to be disposed of, and an increase in the number of contaminated sites." Exh. NRC000012 at 2 (53 Fed. Reg. at 24,019). For that reason, the exemption failed to meet the second part of § 40.14.

Q.48. Why was that not stated explicitly in the April 2011 denial letter?

A.48. (R. Przygodzki) In the letter, we sought to respond to the specific arguments Honeywell made in support of its 2009 exemption request. Honeywell argued that the exemption would be in the public interest, and we focused on those arguments in our response. Also, regardless of whether we considered the exemption contrary to the public interest or a potential threat to life and property, the underlying concern was the same. Namely, we were concerned that granting the exemption would have increased public risk tied to delays in decommissioning the Metropolis Works Facility. As just mentioned, such a delay could lead to increased public doses

and an increased number of contaminated sites. Exh. NRC000012 at 2 (53 Fed. Reg. at 24,019). These effects are clearly threats to life and property.

Q.49. How could granting Honeywell's 2009 exemption request have endangered life and property where granting Honeywell exemptions in 2007 and 2008 did not?

A.49. (R. Przygodzki, K. Kline, T. Fredrichs) To meet the 10-to-1 test in 2009, Honeywell would have needed to rely on much more goodwill than it did in 2007 and 2008. Because of goodwill's relative illiquidity, allowing Honeywell to rely on that asset class to meet the 10-to-1 test in 2009 presented a much greater risk to life and property than it did in previous years. Furthermore, the uncertainty stemming from the global financial crisis raised new and significant concerns that, should Honeywell experience financial distress, it would not be able to raise enough funds to decommission the Metropolis Works Facility without delay.

Q.50. How does Honeywell's situation compare to other cases in which the NRC has granted an exemption from financial assurance requirements?

A.50. (R. Przygodzki) The NRC has at times granted exemptions that excuse an applicant or licensee from paying unnecessary regulatory costs. However, it is the applicant's burden to prove the costs are truly unnecessary. Here, Honeywell failed to make that showing. Based on the global financial crisis in 2009, growing concerns over the reliability of bond ratings, and Honeywell's sharp decline in tangible net worth—with the last factor translating into a sharp *increase* in the amount of goodwill Honeywell needed to use to meet the 10-to-1 test in Appendix C—the Staff found that the cost of complying with § 40.36(e) could no longer be considered unnecessary. In particular, the Staff found that, based on the dramatic increase in Honeywell's noncompliance with the 10-to-1 part of the Appendix C financial test, granting the 2009 exemption would have presented an unnecessary risk to public health and safety. We therefore concluded that exempting Honeywell from the requirements of § 40.36(e) would unfairly shift the financial risk of decommissioning the Metropolis Works Facility to the public, for the sake of Honeywell's private savings. This is quite different from a situation where the

applicant can demonstrate that its requested exemption will not compromise public health or safety.

Q.51. Policy and Procedure Letter (PPL) 1-58 provides guidance for reviewing exemption requests from materials licensees. Does the April 2011 reconsideration decision address the factors identified in PPL 1-58?

A.51. (R. Przygodzki) PPL 1-58 states, in part, that the Staff should consider whether the applicant has taken “measures as necessary to provide a level of health and safety equivalent to the regulation from which the exemption is being requested.” Exh. NRC000016 at Attachment 1, 1. Compared to the risk associated with an instrument that met all regulatory requirements—for example, a surety bond or letter of credit, or a self-guarantee that complied with Appendix C—in 2009 the risk associated with Honeywell’s proposed financial assurance method was clearly greater. Having a financial instrument that met all regulatory requirements therefore provided a higher level of assurance that funding would be readily available to decommission the Metropolis Works Facility. Accordingly, granting Honeywell’s 2009 request would have failed to provide a level of safety equivalent to that contemplated by § 40.36(e).

Q.52. Is the Staff’s view that Honeywell has to meet the requirements of both § 40.14 and PPL 1-58?

A.52. (R. Przygodzki) No. The test in this case is whether Honeywell’s exemption request meets the requirements of § 40.14. However, § 40.14 is written in general terms. For example, § 40.14 states that the exemption must be “in the public interest.” PPL 1-58 provides guidance for determining when this criterion is met. Where, as here, the proposed financial instrument does not provide a level of safety equivalent to that afforded by § 40.36(e), it should be clear that the exemption is not in the public interest.

Q.53. The next section of the Staff’s April 2011 denial letter discusses the decommissioning planning rule. Why does the Staff discuss this rule?

A.53. (R. Przygodzki, K. Kline) Because Honeywell relied on the proposed rule in support of its 2009 exemption request. In its April 2009 request, Honeywell argued that granting an exemption would be “entirely consistent” with the proposed rule. Exh. HNY000006 at 3. In its October 2009 supplement, Honeywell claimed that an exemption would “satisfy the intent” of the proposed rule. Exh. HNY000008 at 9. Because Honeywell made these arguments, we were forced to address them in both our December 2009 denial letter and in our April 2011 letter.

Q.54. Why wouldn't an exemption be consistent with either the letter or intent of the proposed rule?

A.54. (R. Przygodzki, K. Kline) Because the proposed rule required that, in order to meet the Appendix C test, a licensee must have a minimum tangible net worth. By way of background, the proposed rule was issued as a final rule on June 17, 2011, and it goes into effect on December 17, 2012. Exh. NRC000015 at 1 (76 Fed. Reg. at 35,512). The final rule, like the proposed rule, retains the self-guarantee method in Appendix C. Both versions of the rule also revise the Appendix C financial test so that a licensee can use both tangible and intangible assets to meet the 10-to-1 part of the test. Exhs. NRC000014 at 15 (73 Fed. Reg. 3825) and NRC000015 at 13 (76 Fed. Reg. at 35,524). However, both versions of the rule include an additional requirement that a licensee have a minimum tangible net worth. The minimum amount was originally \$19 million, and it was later increased to \$21 million. One benefit of this requirement is that, even if a licensee has to sell intangible assets or a business line to fully fund decommissioning activities, it could rely on tangible assets to prepare a decommissioning plan or begin the early stages of decommissioning. Honeywell obviously did not meet this minimum tangible net worth requirement in 2009. Thus, we properly rejected Honeywell's claims that its exemption request was consistent with the rule and with the intent of the rule.

Q.55. Did you use the criteria in the proposed rule to reject Honeywell's exemption request?

A.55. (R. Przygodzki) No. We mentioned the proposed rule in our December 2009 and April 2011 decisions because Honeywell cited the proposed rule in support of its exemption request.

If Honeywell had not relied on the proposed rule, there would have been no need for us to address it. However, because Honeywell claimed its request was consistent with the rule or with the intent of the rule, the Staff responded to those claims.

Q.56. Now let's turn to Honeywell's June 22, 2011 hearing request. At page 4, Honeywell states that when granting the 2007 and 2008 exemptions the NRC "deemed these assets (tangible assets plus goodwill) sufficient to assure decommissioning funds in times of financial distress." Is that true?

A.56. (R. Przygodzki, K. Kline, T. Fredrichs) No. The Staff previously looked to both Honeywell's tangible net worth including goodwill *and* its bond ratings when evaluating its ability to fund decommissioning activities in times of financial distress. This is stated clearly in the Technical Evaluation Report (TER) accompanying the 2007 renewal of Honeywell's license. In the TER, the Staff states that an "'A' bond rating *and* the high ratio of [tangible] net worth (including goodwill) to decommissioning obligation" provides adequate assurance "that assets will be available for decommissioning in the event of financial distress. . . ." Exh. HNY000009 at 53 (emphasis added). Honeywell's statement in its hearing request omits the bond rating criterion. This is significant, because by 2009 the Staff had strong reasons to question the reliability of bond ratings and, accordingly, strong reasons to question the basis for the prior exemptions.

Q.57. On page 6 of its hearing request, Honeywell states that in the January 2008 proposed decommissioning planning rule, "[t]he NRC proposed to adopt [Honeywell's] alternate financial test used for MTW with respect to the value of goodwill." Is this correct?

A.57. (R. Przygodzki, K. Kline, T. Fredrichs) No. First, when granting the 2007 and 2008 exemptions, the Staff did not adopt a so-called "alternate financial test." If there were an alternate test, it would be included in Appendix C. What the Staff actually did is make fact-specific determinations, based on the information available at the time, as to whether it could grant exemptions in 2007 and 2008. Before the D.C. Circuit, Honeywell similarly tried to argue

that the Staff had previously adopted an alternate test on Honeywell's behalf. However, in its remand order, the D.C. Circuit avoided describing the prior exemptions as being made under an "alternate test."

Second, Honeywell's characterization of the proposed rule ignores other changes that the Staff proposed in January 2008. Significantly, the Staff added a requirement that to self-guarantee a licensee would need a minimum of \$19 million in tangible net worth. Honeywell obviously did not meet that criterion for 2009. Because Honeywell's "alternate financial test" did not include a requirement that it have a minimum tangible net worth, and because such a requirement was included in the proposed rule, it would be more accurate to say that the NRC proposed *rejecting* Honeywell's test.

Q.58. On pages 7 and 8 of its hearing request, Honeywell claims that its 2009 exemption request "was nearly identical to the 2008 request." Was it?

A.58. (R. Przygodzki, K. Kline) No. As we've discussed, between its 2008 and 2009 exemption requests Honeywell experienced a sharp decline in tangible net worth. As a result, in 2009 Honeywell would have needed to rely on significantly more goodwill, and a significantly higher percentage of its goodwill, to meet the 10-to-1 tangible net worth test in Appendix C. This distinguishes the 2008 exemption request from the 2009 request. Further, even if Honeywell's financial data had been similar to that of the previous year, the Staff would have denied the 2009 request. Honeywell's 2009 request came during a global financial crisis. The regulatory context of the exemption requests had thus changed significantly. During late 2008 and continuing throughout 2009, the stability of the global economy was abruptly interrupted by the economic and financial downturn. This created extremely high uncertainty for future business and economic conditions. In brief, the 2009 request was not identical to the 2008 request, nor was the context in which the Staff reviewed the two requests.

Q.59. At pages 10 and 12 of its hearing request, Honeywell refers to a March 2011 meeting at which it presented additional information to the Staff. Honeywell claims this information was

relevant to the Staff's April 2011 reconsideration decision, but ignored by the Staff. Could you comment?

A.59. (R. Przygodzki, K. Kline) We both attended the March 2011 meeting. Our recollection is that prior to the meeting the Staff specifically told Honeywell that we did not intend to discuss the 2009 exemption request. Rather, we agreed to meet with Honeywell in order to gain an understanding of Honeywell's possible support for a future exemption request. In any event, the new information Honeywell presented in connection with the meeting, including its end-of-year 2010 financial data, was irrelevant to our reconsideration decision. Because this information was not available when we issued our December 11, 2009 decision, it would not have helped us decide whether that decision was correct or incorrect.

Q.60. At page 12 of its hearing request, Honeywell argues that in 2009 the Staff ignored the test it applied previously in evaluating Honeywell's requests, a test that looks to the ability to pay decommissioning costs in normal circumstances and in times of financial distress. Did the Staff change its approach when reviewing the 2009 exemption request?

A.60. (R. Przygodzki) No. The Staff continued to look at Honeywell's ability to pay decommissioning costs in normal circumstances and in times of financial distress. We refer to those factors on pages 4 and 6 of our April 2011 denial letter. Obviously, when reviewing the 2009 exemption request, our main concern was with Honeywell's ability to pay decommissioning costs in times of financial distress. We previously found that Honeywell's bond ratings and tangible net worth plus goodwill offered sufficient assurance in this area. In our April 2011 letter, we explain why that reasoning no longer applies.

Q.61. At page 13 of its hearing request, Honeywell claims that in denying the 2009 exemption request the Staff "made unsupported statements regarding the risk of default for companies with an 'A' bond rating." Did you?

A.61. (R. Przygodzki) No. In the April 2011 denial letter, we did not state that the risk of default for "A" rated companies is higher than published. Rather, we stated that an "A" bond

rating, by itself, does not provide sufficient financial assurance to warrant granting an exemption. This finding is no different than the finding reflected in Appendix C itself. If an “A” bond rating were that strong an indicator of the ability to self-guarantee decommissioning funding, there would be no need for an applicant to meet the first two criteria in the Appendix C financial test in order to self-guarantee.

In our April 2011 letter we acknowledged the historically low rate of default for companies with “A” bond ratings. However, as explained in the letter, we were highly concerned about the possibility of increased defaults over the period covered by Honeywell’s 2009 exemption request. Our concern reflected the significant economic uncertainty resulting from the global financial crisis that was still underway when we were reviewing the 2009 exemption request.

Q.62. Also at page 13 of its hearing request, Honeywell claims that in its reconsideration decision the Staff “relied on a proposed \$21 million minimum tangible net worth criterion.” Did you?

A.62. (R. Przygodzki) No. We mentioned the minimum tangible net worth criterion only to rebut Honeywell’s argument that its requested exemption was consistent with the proposed rule. If we did not do so, Honeywell could have claimed that we failed to respond fully to its arguments.

Q.63. In its remand order, the D.C. Circuit raised a number of questions regarding how the Staff weighed tangible net worth and goodwill when reaching its December 2009 denial decision. Could you summarize how you have addressed those concerns?

A.63. (R. Przygodzki) First, our decision does not depend entirely on Honeywell’s multi-billion-dollar decline in tangible net worth between its 2008 and 2009 exemption requests. When we granted exemptions in 2007 and 2008, Honeywell’s bond ratings were an integral part of our decisions. By late 2008 and 2009, however, the global financial crisis forced us to question the reliability of bond ratings as a primary measure of a company’s ability to provide financial

assurance. The ongoing financial crisis, coupled with the growing questions about the reliability of bond ratings, therefore removed critical support for Honeywell's prior exemptions.

Second, Honeywell's significant decline in tangible net worth meant that, for 2009, Honeywell would have needed to rely on significantly more goodwill to meet the 10-to-1 test. For several reasons, we had a heightened concern over Honeywell's reliance on goodwill. Honeywell would have needed to use an unprecedented amount of its goodwill—almost \$7 billion—just to meet the 10-to-1 test. This was a significant increase over 2008, when Honeywell needed only \$3.7 billion to meet the test. Exhs. NRC000018 and NRC000021. Honeywell's increased reliance on goodwill was of great concern because goodwill is illiquid relative to other assets and therefore might not be readily available to fund decommissioning activities. Furthermore, Honeywell would have needed to apply 67% of its goodwill toward meeting the 10-to-1 test in 2009, up from 40% the prior year. Exhs. NRC000018 and NRC000022. Because of the risk of goodwill impairment in an unstable global market, this was an additional concern for the Staff. We were particularly concerned that, if Honeywell fell into financial distress and had to sell off goodwill quickly, it might realize far less than book value for its goodwill.

In addition, Honeywell's ratio of tangible net worth to decommissioning expenses declined significantly by the time it sought the 2009 exemption. Honeywell's ratio went from positive 7.9-to-1 to negative 6.5-to-1 to negative 33.7-to-1 over the three years it requested exemptions. Exhs. NRC000018 and NRC000020. This pushed Honeywell much further out of compliance with the 10-to-1 test in Appendix C, and it established that Honeywell would not soon return to compliance with that test. Honeywell's explanation of one of the reasons for its noncompliance—that it was actively increasing its goodwill despite the effect on tangible net worth—reinforced our conclusion.

Q.64. Does the Staff have any test for balancing goodwill against tangible net worth when reviewing an exemption request similar to Honeywell's?

A.64. (R. Przygodzki) No. If there were such a test, it would be—or should be—in Appendix C itself. The Staff reviews exemption requests by considering all factors relevant to a specific request. In Honeywell's case, we considered factors such as general economic conditions, the reliability of bond ratings, and the relative illiquidity of goodwill compared to other assets. In brief, when reaching our April 2011 decision we considered all factors cited by Honeywell in its exemption request, and all other relevant factors.

Q.65. Does this conclude your testimony?

A.65. (R. Przygodzki, K. Kline, T. Fredrichs) Yes.