UNITED STATES OF AMERICA
NUCLEAR REGULATORY COMMISSION

Before the Director of the Office of
Nuclear Reactor Regulation

In the Matter of	)	
	)	
ALABAMA POWER COMPANY	)	Operating Licenses
	)	
(Joseph M. Farley Nuclear	)	Nos. NPF-2 and NPF-8
	)	
Plant, Units 1 and 2)	)	
	)	

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MEMORANDUM OF ALABAMA POWER COMPANY IN RESPONSE TO REQUEST OF ALABAMA ELECTRIC COOPERATIVE, INC. FOR ENFORCEMENT ACTION

I. INTRODUCTION

On June 29, 1984, Alabama Electric Cooperative, Inc. ("AEC"), requested, pursuant to Section 2.206 of the Commission's Rules of Practice, that the Director, Office of Inspection and Enforcement, take enforcement action against Alabama Power Company ("APCO"), including imposition of civil penalties and suspension of APCO's licenses to operate the Joseph M. Farley Nuclear Plant, Units 1 and 2 ("Plant Farley") for its purported "willful and continuing violation of Antitrust License Condition No. 2." This license condition (the "License Condition") was imposed as a result of a decision by the NRC's Atomic Safety and Licensing Appeal Board issued on June 30, 1981. 1/ The License

1/ Alabama Power Company (Joseph M. Farley Nuclear Plant, Units 1 and 2), ALAB-646, 13 NRC 1027 (1981), aff'd, Alabama Power Company v. Nuclear Regulatory Commission, 692 F.2d 1362 (11th Cir. 1982), cert. denied, 104 S.Ct. 72 (1983).

Condition, which was incorporated into the license on August 10, 1981, reads, in pertinent part, as follows:

> 2. Licensee shall offer to sell to AEC an undivided ownership interest in Units 1 and 2 of the Farley Nuclear Plant. The percentage of ownership interest to be so offered shall be an amount based on the relative sizes of the respective peak loads on AEC and the Licensee (excluding from the Licensee's peak load that amount imposed by members of AEC upon the electric system of the Licensee) occuring in 1976. The price to be paid by AEC for its proportionate share of Units 1 and 2, determined in accordance with the foregoing formula, will be established by the parties through good faith negotiations. The price shall be sufficient to fairly reimbuse Licensee for the proportionate share of its total costs related to the Units 1 and 2 including, but not limited to, all costs of construction, installation, ownership and licensing, as of a date, to be agreed to by the two parties, which fairly accomodates both their respective interests. The offer by Licensee to sell an undivided ownership interest in Units 1 and 2 may be conditioned at Licensee's option on the agreement by AEC to waive any right of partition of the Farley plant to avoid interference in the dayto-day operation of the plant.

AEC contends that APCO has been dilatory in the conduct of negotiations for sale of an interest in Plant Farley and has taken negotiating positions that are inconsistent with good faith negotiation. 2/

APCO urges that AEC's request be denied on the basis that APCO has not violated the License Condition and has acted in good faith in any case. When the negotiations reached an impasse, APCO, desiring to minimize further delay, sought a declaratory order from the NRC interpreting the License Condition. 3/ If the

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2/ Letter to the Director, Office of Inspection and Enforcement from Charles R. Lowman, General Manager of AEC (June 29, 1984). ("AEC Enforcement Action Request").

3/ The Petition of Alabama Power Company for a Declaratory Order, dated July 3, 1984, is attached hereto as Appendix A (footnote continued)

Director concludes that APCO's positions during negotiations have been inconsistent with the License Condition in any respect, the appropriate action would be to inform APCO of the Director's interpretation of the License Condition and to provide APCO with the opportunity either to conform to the Director's interpretation or to seek review of it within the Commission. Certainly, the sort of punitive action sought by AEC would not be appropriate.

In Part II, below, we discuss the legal standards that pertain to the inquiry. In Part III, we address the substance of AEC's allegations and demonstrate that:

o APCO has conducted its negotiations with AEC with diligence and good faith, and has not sought unduly to delay the negotiating process.

o The lack of progress in the negotiation is attributable to AEC's intransigence and refusal to negotiate within the general terms of the License Condition, and there is reason for concluding that AEC has calculatedly sought to delay and frustrate the negotiation.

o APCO's position on the pivotal issue of price is consistent with the License Condition and based upon sound economic, accounting and business considerations.

(footnote continued from previous page)
(excluding the exhibits thereto, virtually all of which are being supplied as attachments to Mr. Franklin's Affidavit).

o Other positions taken by APCO in the negotiation, and challenged by AEC, are commercially reasonable and grounded upon legitimate business considerations.

In order to provide the Director with a complete record, APCO is submitting, in support of this Memorandum, the sworn affidavits of H. Allen Franklin, Dr. Charles Cicchetti, Richard Walker, and Philip Kron. 4/ These affidavits constitute a strong evidentiary basis for disposing, once and for all, of AEC's groundless complaints.

II. LEGAL STANDARDS AND PROCEDURES

AEC's request is before the Director of Nuclear Reactor Regulation ("Director") pursuant to 10 CFR, Part 2, Subpart B, and more particularly 10 CFR § 2.206. The Director, to whom the Commission has delegated its own authority, has broad discretion to consider such facts as he deems relevant and, on the basis of the record before him, to decide whether any sort of enforcement action is required. 5/

Unlike a petition for intervention in a proceeding convened pursuant to Section 186 of the Atomic Energy Act, a person requesting the initiation of an enforcement proceeding is not entitled to a hearing by virtue of meeting certain threshold

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4/ The affidavits of Mr. Franklin, Dr. Cicchetti, Mr. Walker, and Mr. Kron are attached hereto as Appendices B, C, D, and E, respectively.

5/ Porter County Chapter of the Izaak Walton League v. NRC, 606 F.2d 1363 (D.C. Cir. 1979); Illinois v. NRC, 591 F.2d 12 (7th Cir. 1979).

pleading standards. Instead, a request under § 2.206 is addressed to the discretion of the Director, whose only obligation to AEC is to explain his decision and to avoid abusing his discretion. 6/ Therefore, the Director is free to reach his own conclusions as to disputed factual matters, so long as those conclusions are rational, and to deny the request on the basis of his findings. 7/

If the Director concludes that APCO is not in compliance with the License Condition, as interpreted by the Director, the normal procedure is to issue a notice of violation pursuant to 10 CFR § 2.201. The notice of violation affords the licensee an opportunity to avoid issuance of a show cause order by demonstrating or achieving compliance with the license. The NRC's regulations, 10 CFR § 2.201, and the Administrative Procedure Act, 5 U.S.C. § 558, provide that a notice of violation shall be issued at least twenty days before issuance of a "show cause" order pursuant to 10 CFR § 2.206. The Administrative Procedure Act sets forth the procedure, and its underlying rationale, as follows:

> Except in cases of willfulness or those in which public health, interest or safety requires otherwise, the withdrawal, suspension, revocation, or annulment of a license is lawful only if, before the institution of agency proceedings . . . the licensee has been given notice by the agency in writing of the facts or conduct which may warrant the

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6/ See Consolidated Edison Co. of New York (Indian Point, Units 1, 2 and 3), CLI-75-8, 2 NRC 173 (1975).

7/ Id.

> action; and opportunity to demonstrate or achieve compliance with all lawful requirements.

If the Director is not satisfied with the licensee's response to the notice of violation, the Director may issue an order, under 10 CFR § 2.202, requiring the licensee to show cause why specified enforcement action should not be taken. If, at this stage, the licensee believes that it is not in violation of the license, it may request a trial type hearing, in which the proponents of the enforcement action would bear the burden of establishing the alleged violation. 8/

APCO believes that the response to AEC's allegations contained in this Memorandum and the attached affidavits provides an ample basis for outright denial of AEC's request on the ground that APCO has fully complied with the License Condition. If, notwithstanding the showing made by APCO, the Director believes that APCO has not yet fully discharged its obligations under the License Condition, any action taken should be interpretive rather than punitive in its effect, and APCO should be accorded all procedural rights available to a licensee that has not willfully violated the terms of its license.

8/ See 10 C.F.R. § 2.732

III. APCO HAS ENDEAVORED IN GOOD FAITH TO IMPLEMENT THE LICENSE CONDITION AND AEC'S CLAIMS TO THE CONTRARY ARE WITHOUT MERIT

AEC asserts that enforcement proceedings should be initiated because APCO has not made a good faith effort to comply with the License Condition. It makes two basic arguments in support of this contention: (1) the history of negotiations demonstrates APCO's procrastination and half-hearted participation in negotiations; and (2) the terms proposed by APCO are, in themselves, so unreasonable as to indicate bad faith. As demonstrated below, neither of these arguments has merit.

A. APCO Has Negotiated in Good Faith, Faced with AEC's Intransigence and Bad Faith

1. APCO has Pursued Negotiations with Diligence and Good Faith

The history of the negotiations between the parties is recounted in detail in the attached Affidavit of H. Allen Franklin, an Executive Vice President of Southern Company Services, Inc., who has been involved in each step of these negotiations, and is summarized below.

Promptly after the NRC denied APCO's requested stay of the Appeal Board's order incorporating the License Conditions into the licenses for Plant Farley, APCO agreed to supply AEC with the information the latter required to begin negotiations. 9/ Even

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9/ Franklin Affidavit, p. 6. Much earlier, in 1977, APCO had offered to share cost information relating to the plant with AEC and to begin negotiations with AEC to implement the license conditions imposed by the Atomic Safety and Licensing Board in its Initial Decision. Alabama Power

(footnote continued)

prior to that time, APCO had been engaged in a review of contractual arrangements for other sales by electric utilities of ownership interests in nuclear power plants. Id., p. 7. Following APCO's provision of data, AEC assigned its consultants to gather and analyze a substantial amount of information, and began its analysis. In June 1982, AEC informed APCO that AEC would indicate when it had completed review of the information and was prepared to begin substantive negotiations. Id.

AEC's review of information continued until March 1983, and Mr. Franklin's affidavit confirms that APCO expended considerable effort to comply with the requests of AEC's consultants, who often sought information in a form not readily available from APCO's records. 10/ Undoubtedly, a substantial amount of AEC's attention was concentrated, during that period, on proceedings pending in the United States Court of Appeals for the Eleventh Circuit on review of the NRC's decision that resulted in imposition of the License Condition. Those proceedings culminated in issuance, on December 6, 1982, of a decision upholding the NRC's order. Alabama Power Company v. NRC, 692 F.2d 1362 (11th Cir. 1982).

(footnote continued from previous page)
Company (Joseph M. Farley Nuclear Plant, Units 1 and 2), LBP-77-24, 5 NRC 804 (1977). AEC, which was dissatisfied with the conditions framed by the Licensing Board, indicated no interest at all in pursuing such negotiations. Franklin Affidavit, pp. 4-5.

10/ Id., pp. 6-7.

Promptly after receiving, in March 1983, notification that AEC was prepared to begin substantive negotiations, APCO submitted its initial offer, which included a proposed sales price and a summary of major contractual terms. 11/ The parties met on several occasions between May and September, 1983. The substance of these discussions is summarized in a letter dated September 26, 1983, from Jesse S. Vogtle of APCO to Charles R. Lowman of AEC. 12/ Although progress was made on some issues, no progress at all was made on the pivotal issue of the sales price. AEC flatly rejected APCO's offer and took the position that it would pay no more than the cost that it would have incurred had APCO sold AEC an interest at some unspecified time in the early 1970s. 13/ AEC first took this stand in a letter dated June 4, 1982, and continues to adhere to that position today, 14/ although it has never quantified the price that it would deem acceptable. 15/

11/ Letter of April 29, 1983, from Jesse S. Vogtle to Charles Lowman. Id., Attachment 3.

12/ Id., Attachment 9.

13/ Id., pp. 27-29.

14/ AEC Enforcement Action Request, p. 6.

15/ Franklin Affidavit, p. 28. AEC provided to APCO, in January, 1984, a draft of an ownership agreement which omitted any specification of the sales price and which failed to include essential terms of such an agreement.

Since September 1983, APCO has prepared and offered to AEC comprehensive Ownership, Operating, and Nuclear Fuel Agreements. 16/ APCO has also continued to meet with AEC to discuss areas of disagreement, and even took the initiative of opening a second, less formal, negotiating channel in the hope of advancing the process. 17/

AEC advances three specific charges in support of its claim of procrastination on APCO's part. First, it asserts that, in July 1981, APCO refused to initiate discussions with AEC. However, AEC admits that the License Condition was not yet in effect at that time. 18/ Second, it claims that, after the condition took effect, data was not forthcoming from APCO as promptly and in as much detail as AEC might have desired. However, the claimed delays are de minimis, particularly in the context of the leisurely pace at which AEC reviewed the data supplied by APCO. 19/ Third, AEC quotes, as alleged evidence of the "foot-dragging and bad faith tenor of APCO's approach to discussions," language from APCO letters that was intended to

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16/ These agreements are Attachments 10, 11, and 12, respectively, to the Franklin Affidavit.

17/ Id., p. 29.

18/ AEC Enforcement Action Request, pp. 2-3. On August 10, 1981, the NRC informed APCO that the License Condition was incorporated into the license for Plant Farley.

19/ AEC contends that a data request transmitted to APCO in October 1981 was not responded to until November 1981 and that it was necessary for AEC, in January 1982, to request "clarifications and explanation," a request to which APCO responded in February, 1982. Id., p. 3.

preserve APCO's appellate rights with respect to the NRC decision. 20/ However, as the Department of Justice acknowledged in pleadings filed in response to APCO's motion for a stay of the NRC order imposing the License Condition, it was entirely appropriate for APCO to condition its offer to AEC upon the outcome of appellate proceedings. 21/

The foregoing demonstrates that APCO has not procrastinated and has pursued negotiations in good faith.22/ The lack of progress in negotiations is due not to procrastination or indifference on APCO's part, but to AEC's steadfast refusal to negotiate on critical issues, particularly the sales price.

2. AEC Has Acted in Bad Faith and Sought to Frustrate the Negotiating Process

In the section that follows we will address in detail the reasonableness of APCO's initial offer. However, whatever one's view of the appropriate terms that should have emerged from the negotiating process, it is clear that APCO sought actively to negotiate the sales price issue. APCO came forth with a detailed offer and characterized its offer as an opening negotiating

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20/ AEC Enforcement Action Request, pp. 3-4.

21/ "Memorandum for the United States and the Nuclear Regulatory Commission in Opposition", S.Ct. Docket No. 82-1788 (April 1983), p. 3.

22/ Attached hereto as Appendix F is a time line which displays graphically the major events that have occurred in the course of the Company's attempts to implement license conditions imposed by the Licensing Board and the Appeal Board with respect to access to the Farley Plant. This Appendix reflects that during most of the interludes, the ball was in AEC's court.

position. 23/ AEC never submitted its own price proposal, and never directly took issue with the components of APCO's offer. 24/

Moreover, AEC took, and doggedly adhered to, a position that is blatantly inconsistent with the terms of the License Condition: that APCO is not entitled to recover its actual cost of capital incurred during construction of the two units. In a letter dated October 11, 1983, AEC told APCO that it interprets the License Condition as providing "that AEC's share of the units is to be purchased at AEC's cost of capital. . ." incurred prior to the date of sale, i.e., AEC would calculate the sales price as if AEC had bought into the units prior to commencement of construction and had contributed capital, acquired at the relatively low cost at which REA cooperatives are able to borrow money, throughout the process. This "retroactive sale" theory cannot be squared with the plain words of the License Condition, which provide that the sales "price shall be sufficient to fairly reimburse Licensee for the proportionate share of its total costs related to the Units 1 and 2."

AEC's position cannot have been taken in good faith. The position that APCO should not recover its costs of funds used during construction is plainly inconsistent with the words of the License Condition and with the decisions of the NRC's Appeal

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23/ Franklin Affidavit, p. 16.

24/ Id., p. 29.

Board 25/ and the United States Court of Appeals for the Eleventh Circuit, which affirmed the NRC's decision on the basis that the License Condition provides for APCO to recover the "reasonable value" of the interest sold to AEC. 26/ AEC's position on price assumes that the NRC intended that the License Condition would operate in a punitive manner, an intent that finds no support in the Appeal Board's decision and is inconsistent with the spirit of Section 105c, which was enacted to prevent future conduct inconsistent with the antitrust laws rather than to punish past conduct. 27/

Perhaps the most telling evidence of AEC's bad faith is that the position that it now advances flatly contradicts the representations that AEC made to the NRC's Licensing Board in its brief in the relief phase of the proceeding. Arguing for imposition of a license condition requiring that APCO offer to sell an ownership interest, in contrast with unit power, AEC represented that:

25/ Had the Appeal Board intended to order a sale retroactive to some date in the early 1970s, it would have said so. Moreover, it would have made findings as to the date when APCO's refusal of an offer by AEC took place and specified the date as of which the sales price would be calculated. It did not do so.

26/ 692 F.2d at 1367. The government gave assurance in its brief to the Eleventh Circuit that "[e]ach condition placing an affirmative duty on APCO . . . also provides that APCO is to be fully compensated and that reliability of service to its customers is not to be impaired." DOJ Brief at 61.

27/ It is the key purpose of prelicensing antitrust review to "nip in the bud any incipient violations." Joint Committee Report, p. 14.

> In a joint ownership venture each party contributes to the real cost of the facility on the basis of its proportion of the facility's costs (burdens) and receives from the facility its proportionate share of its production (benefits). AEC under these standards should be entitled to purchase a reasonable share of the facilities at their actual cost (including such interest during construction actually booked), and to pay for at actual cost such fuels, materials, supplies and other items.

AEC Brief at 21. (Emphasis added). The relief sought by AEC was characterized as "tailored to fence in the monopoly power found to exist and to foreclose for the future the types and forms of conduct found to have been engaged in by the wrongdoer, thereby prying open the monopoly lock on market place competition. The function of antitrust remedy in the context of this proceeding is not punishment...." AEC Brief at 14. 28/

3. APCO Has Every Incentive to Complete the Sale Promptly, While AEC's Interest Would be Served by Delay

Once the NRC's decision became final, APCO had, and still has, every incentive to implement the License Condition as promptly as possible. As Mr. Franklin testifies, the cost of power from Plant Farley is currently higher than the average cost of power in APCO's system, a situation that is expected to change when a "cross-over" point is reached around 1990. 29/ In effect, APCO and its customers are incurring higher early year costs in

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28/ See also DOJ Brief at 16. The Government concurred that "the purpose of a proceeding under Section 105(c) is clearly not punishment of past misconduct . . ."

29/ Franklin Affidavit, p. 32.

the expectation of having the cost of power on APCO's system reduced for many years after 1990 due to the presence of Plant Farley. 30/ If a portion is to be sold to AEC, APCO and its customers would suffer least from a prompt sale, which would result in AEC beginning to pay its share of costs as early as possible.

On the other hand, from AEC's perspective, the optimal economic scenario would be to continue to purchase wholesale power from APCO, for the substantial portion of AEC's total Alabama load that is now served at wholesale by APCO, until approximately 1990, and only then to purchase an ownership interest in Plant Farley. Mr. Franklin's Affidavit demonstrates that, under any credible scenario, the cost of wholesale power purchased from APCO is now, and for several years will be, lower than the cost of power that could be achieved by AEC from an owernship interest in Plant Farley, even taking into account the substantial tax and capital subsidies available to AEC. 31/ AEC's actions in these negotiations appear to coincide with its economic interest.

In summary, AEC has taken positions in the negotiations that are inconsistent with good faith negotiation. Moreover, evidence indicates that AEC's actions are part of a thoughtful strategy designed to defer purchase of Plant Farley for as long as possible while holding open AEC's "option" to purchase at the

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30/ Id.

31/ Id., p. 31, Attachment 7.

optimal time, and, in the meantime, to utilize the processes of the NRC to obtain as much tactical advantage as possible. In the face of this outrageous conduct, APCO has made a good faith effort to negotiate with AEC the terms of sale of an interest in Plant Farley. The record to date demonstrates only that a fruitful negotiation cannot be created by APCO unilaterally.

B. APCO's Negotiating Position on the Issue of Sales Price Has Been Consistent with the Express Terms of the License Condition and Reasonable by Commercial Standards

The License Condition requires APCO to offer to sell to AEC an ownership interest in Plant Farley at a price, to "be established by the parties through good faith negotiations", which will "be sufficient to fairly reimburse Licensee for the proportionate share of its total costs related to the Units 1 and 2 including, but not limited to all costs of construction, installation, ownership and licensing, as of a date, to be agreed to by the two parties, which fairly accommodates both their respective interests." (Emphasis added). On review of this condition, the Court of Appeals for the Eleventh Circuit characterized it as requiring AEC to pay reasonable value. Alabma Power Company v. NRC, 692 F.2d at 1367. A discussion of the price issue appears to be divisable into three parts. First, is APCO required by the license condition to offer to sell at a price below APCO's actual costs up to the date of the sale, as AEC insists? Second, is APCO's effort to bargain for a price comparable to that which would prevail in a commercial trans-

action where a willing seller negotiated with willing buyers inconsistent with the License Condition's requirement for "good faith negotiations" and with the Eleventh Circuit's interpretation of the condition? Third, how does APCO's current offer stack up against the measures identified in the first two questions: cost, and fair market value?

1. APCO is Not Required to Sell Below Its Actual Costs

AEC's position, now and throughout the negotiations, is that APCO is entitled to recover the costs reflected on its books, except that, instead of recovering the cost that APCO actually incurred for funds used during construction, it should receive a lesser amount calculated on the basis of the cost of capital that AEC would have incurred had it infused capital from the outset of construction of each unit of Plant Farley. AEC has not come forth with a calculation quantifying the effect of application of this theory; 32/ however, clearly it believes that adoption of its theory would result in a sales price below APCO's cost. 33/

32/ AEC has also failed to provide APCO with the information necessary to make such a determination.

33/ It is not at all clear that this would be the case if a retroactive sale theory were to be applied with consistency. For example, if the sale were priced as if made in the early 1970s it would be improper to reduce APCO's investment (exclusive of cost of capital) by any allowance for depreciation. Moreover, AEC could not logically retain both the advantage associated with purchase of Plant Farley a decade ago and the cost advantage that it has derived from wholesale power purchases that would have been displaced by AEC's interest in Plant Farley.

The response to AEC's contention is a simple one. The License Condition requires that the price be "sufficient to fairly reimburse Licensee for the proportionate share of its total costs . . ." The cost of capital used during construction is indisputably part of APCO's "total costs." Even if the License Condition were less clear on this point the result would be the same, for at least three reasons, each of which was touched upon in III, A, 2, above. In summary:

a. Requiring that APCO sell an interest at a price below its actual cost would be punitive toward APCO and amount to a damage award in favor of AEC. This is inconsistent with the theory of Section 105c, which is preventive and prospective in nature and permits the NRC to look only "for 'reasonable probability' of violation. This command may result in the conditioning of licenses in anticipation of situations which would not, if left to fruition, in fact violate any antitrust law." 34/ Moreover, if the NRC had meant to assess a penalty, it hardly would have left determination of the amount of the penalty to "good faith negotiations" between the parties. In any case, courts have consistently held that administrative agencies are prohibited from ordering damage awards, absent explicit legislative authorization. See, for example, Heater v. FTC, 35 Ad. L 2d 663 (9th Cir. 1974), holding that the FTC does not

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34/ Alabama Power Company v. NRC, 692 F.2d at 1368. See also Joint Committee Report at 14; Hearings, Pt. 1, at 124-126.

possess the authority to require a person, found to be using an an unfair method of competition, to make restitution of the moneys secured thereby. 35/

b. Parties to the proceeding under Section 105c seeking the imposition of license conditions represented to the Licensing and Appeal Board that the relief they sought would not operate in a punitive fashion and, indeed, that APCO would not be disadvantaged by such relief. 36/ With this record before it, the Appeal Board said nothing that suggests that it had an entirely different result in mind.

c. The NRC and the Department of Justice, in their brief arguing for affirmance of the NRC's decision, represented to the Eleventh Circuit that, under the License Condition, APCO would be fully compensated for the interest that it is required to offer to AEC. 37/ The Eleventh Circuit relied on this representation, holding that "AEC would, of course pay the reasonable value for this interest." 692 F.2d at 1367.

In summary, AEC has confused its undisputed right to enjoy the benefit of its lower capital cost rate from and after the date of the sale with APCO's right, at a minimum, to be compensated for the costs that it has actually incurred up to the time

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35/ See also Montana-Dakota Utilities Co. v. Northwestern Public Service Co., 341 U.S. 246, 254 (1951) ("Congress withheld from the Commission power to grant reparations").

36/ See discussion at page 13.

37/ See supra note 26, at 12.

of the sale. The License Condition, and the record of the proceeding in which it was imposed, are unmistakably clear on both points.

2. The License Condition Does Not Prohibit APCO from Seeking a Price Based on Fair Market Value

While the License Condition assures that APCO will receive a price "sufficient" to reimburse it for its total costs associated with the interest sold to AEC, it does not require APCO to limit its offer strictly to recovery of costs. This appears to have been quite deliberate. The condition issued by the Licensing Board following the remedy phase of the antitrust hearings, which required a sale of unit power to AEC, expressly provided that "AEC will pay its proportionate share of Licensee's total costs related to such nuclear units including, but not limited to, all costs of construction, installation, ownership, licensing and operation of such units, but no more than such proportionate share." 38/ [Emphasis added]. The License Condition adopted by the Appeal Board provides a substantial advantage to AEC, as compared with the condition framed by the Licensing Board, in that, following the sale, AEC will have the considerable benefit of its lower cost of capital. However, the Appeal Board omitted from its condition the language underlined above and added the requirement that the sale price "be established by the parties

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38/ Alabama Power Co. (Joseph M. Farley Nuclear Plant, Units 1 and 2), LBP-77-41, 5 NRC 1482, 1507 (1977).

through good faith negotiations," a provision which would be superfluous if the License Condition were intended to prescribe a single, mathematically ascertainable sale price.

In adopting this approach, the Appeal Board acted consistently with the theory underlying the divestiture remedy that has been developed by the federal courts. The principle remedial objective of divestiture is to forestall future anticompetitive uses of increased market power. International Salt Co., Inc. v. United States, 332 U.S. 392 (1947). Divestiture is not, however, a penal remedy and the "relief must not be punitive." United States v. E.I. DuPont de Nemours, 366 U.S. 316, 326 (1961). Therefore, among the factors to be considered in framing a divestiture decision is "the effect on private property." Kintner, Primer on the Law of Mergers (1973), at 187. The courts have applied this principle to protect defendants from divestment of assets at less than their fair market value.

Thus, both with respect to consent decrees, 39/ and in cases of divestiture ordered after trial, 40/ the courts have recognized fair market value as the proper measure of compensation to the divesting firm. Moreover, no court has taken

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39/ See, e.g., United States v. Maremont Automotive Products, Inc., 1960 Trade Cas. (CCH) ¶ 69, 881 (N.D. Ill. 1960), where the consent judgment required divestiture upon terms and conditions "having due regard...for the fair market value of the assets...." 1960 Trade Cas. at p. 77, 501.

40/ See United States v. El Paso Natural Gas Co., 358 F. Supp. 820, 826 (D. Colo. 1972), aff'd, 410 U.S. 962 (1973), where the court held that "the basis for reimbursement to El Paso for the divested assets should be the fair market value...as determined by the court."

enforcement action against a defendant for failure to divest in compliance with a decree, except in situations where the defendant insisted, unreasonably and in bad faith, on a sales price clearly above fair market value. See Pfunder, Plaine & Whittemore, Compliance with Divestiture Orders Under Section 7 of the Clayton Act: An Analysis of Relief Obtained, 17 Antitrust Bull 19, 82 (1972). In United States v. Papercraft Corporation, 393 F. Supp. 415 (W.D. Pa. 1975), for example, the court imposed civil penalties on Papercraft for violation of an FTC divestiture order, on findings that it "only sought a sale transaction at an unreasonably high price." Id. at 420. Papercraft initially set an asking price of $37.5 million for the assets subject to divestiture, which was seven times the acquisition cost and twenty times its most recent yearly earnings. Papercraft's own consultant appraised the value of the assets at $14.9 million. Offers for the assets at issue ranged between $13 million and $25 million, but never approached Papercraft's asking price. The court concluded that, since defendant's proposals were "unreasonably above any market interest", Id. at 424, noncompliance with the divestiture order was established.

A similar example of the use of the fair market value standard to evaluate a defendant's divestiture efforts is United States v. Louisiana-Pacific Corporation, 554 F. Supp. 504 (D.Or. 1982), where the court imposed a civil penalty for violation of an order to divest a manufacturing plant. According to the

court, and based upon expert testimony 41/ of "an estimated sale price fair value of $20 million", 554 F.Supp. at 508, a fair price was $20 million and the defendant's asking price of $40 million was unreasonable, indicating "a failure to make good faith efforts to comply." Id. at 510. We are aware of no case in which a court has made such a finding with respect to a sales offer which was considered to be a reasonable estimate of fair market value.

Clearly, the Eleventh Circuit read the License Condition as a typical antitrust divestiture condition, as it stated that "AEC would, of course, pay the reasonable value for this interest." 692 F.2d at 1367.

Decisions arising under the so-called essential facility doctrine, although not directly pertinent, also provide that when a company in control of such a facility is required to make access available to competitors, the terms of access must be "fair and reasonable." 42/ In its decision imposing the License Condition the Appeal Board did not characterize Plant Farley as an "essential facility" or base its action on that doctrine. In light of the evidentiary record demonstrating that any near-term

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41/ Where the market mechanism has failed to provide an adequate basis for determining the reasonableness of the asking price, courts have relied upon expert testimony. See Louisiana-Pacific Corporation, supra; United States v. United Foam Corporation, 1980-1 Trade Cas. (CCH) ¶ 63, 326 (9th Cir. 1980).

42/ United States v. American Telephone & Telegraph Co., 524 F. Supp. 1336, 1352-53 (D.D.C. 1981), citing United States v. Terminal R.R. Ass'n., 224 U.S. 383 (1912).

cost advantage from Plant Farley was considered to be problematical, such a finding would not have been sustainable. Moreover, the License Condition requires APCO to divest capacity that is now being fully utilized by APCO, a result that could not be supported by the "essential facility" cases. 43/ As is the case with respect to the divestiture remedy, relief in the form of access to an essential facility is not intended to operate punitively: "The essential facility analysis exists not to punish a monopolist for anticompetitive behavior, but to provide a remedy to a party denied access to an essential facility." Troy, Unclogging the Bottleneck: A New Essential Facility Doctrine, 83 Colum. L. Rev. 441, 470 (1983). 44/

We have found no case in which a court has actually prescribed the terms on which access to an essential facility is to be made available. However, there is no reason for believing

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43/ See MCI Communications Corporation v. American Telephone & Telegraph Co., 708 F.2d 1081, 1133 (7th Cir. 1983); Town of Massena v. Niagara Mohawk Power Corporation, 1980-2 Trade Cas. (CCH) ¶ 63,526 (N.D.N.Y. 1980); Gamco, Inc. v. Providence Fruit and Produce Building, Inc., 194 F.2d 484 (1st Cir.), cert. denied, 344 U.S. 817 (1952); Southern Pacific Communications Co. v. American Telephone and Telegraph Co., 556 F.Supp. 825 (D.D.C. 1983), affirmed, Southern Pacific Communications Co. v. AT&T, 740 F.2d 980 (D.C. Cir. 1984). These cases establish that the owner of such a facility is under no obligation to make access available to others if the owner requires the capacity for its own use, which is the case with respect to APCO's utilization of Plant Farley.

44/ See also Mid-South Grizzlies v. National Football League, 720 F.2d 772 (3d Cir. 1983), cert. denied, 104 S. Ct. 2657 (1984). ("The essential facilities doctrine is predicated on the assumption that admission of the excluded applicant would result in additional competition.")

that a court would apply any standard other than the fair market value standard applied in divestiture cases. The one treatise writer who has addressed the subject rejects the view that the court in the seminal Terminal Railroad case 45/ intended to establish a requirement that access be based on the costs of the firm owning the facility, concluding that such a rule would reduce incentives for superior performance 46/ -- a consideration that is apposite in this case, where the market value of Plant Farley has been enhanced by APCO's superior record in management of construction and in operation of the plant. Dr. Charles Cicchetti's testimony reveals his agreement with this evaluation. 47/

The terms of the License Condition, the construction given the License Condition by the Eleventh Circuit, and the standards applied by the courts all lead to the same result. 48/ The

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45/ See United States v. Terminal R.R. Ass'n, 224 U.S. 383, 411 (1912), where the Court ordered that competitors be allowed the option of purchasing an interest in or being permitted to use defendant's strategically located railroad terminal.

46/ Sullivan, Handbook of the Law of Antitrust, § 48 (1977) at 126. In the one instance in which Professor Sullivan discusses cost concepts, where a firm has been excluded from a joint venture involving an essential facility, he emphasizes that it is necessary "to allow the original investors an adequate return upon their earlier investment, predicated upon the risk elements which it involved." Id. at 132.

47/ Cicchetti Affidavit, p. 8.

48/ As noted above, AEC contends that the License Condition is intended to restore it to the position that it would have occupied if it had bought an interest in Plant Farley in the early 1970s. AEC, however, confuses the access, or

(footnote continued)

License Condition should be construed to give AEC an opportunity for access to nuclear power on the terms that would prevail in a commercial environment in which willing buyers deal with willing sellers. In such a free, competitive marketplace assets are sold at the fair market value at the time of sale. Accordingly, the appropriate standard for judging APCO's compliance with the License Condition is: does APCO's offer clearly exceed the current fair market value of Plant Farley?

c. APCO's Sale Price Proposal is Reasonable and Consistent with the License Condition

In the offer that it transmitted to AEC in April 1983, APCO proposed to sell an ownership interest in Plant Farley for $1568 per kw of capacity. 49/ Mr. Franklin describes the derivation of

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(footnote continued from previous page)
divestiture, remedy, which is intended to have prospective effect, with compensation for damages allegedly suffered by AEC for what it asserts was an unlawful refusal by APCO to sell AEC an interest in Plant Farley in the early 1970s, long before the License Condition was in effect. The proper forum for the latter issue is a private damage action in a United States District Court, a course that AEC has been free to attempt at any time. However, in a civil antitrust action AEC must establish a violation of the antitrust laws, in contrast with the broader standard that the Eleventh Circuit found applicable under Section 105c. The only federal court that has addressed a claim that a refusal to sell an ownership share of a nuclear power plant is an antitrust violation disposed of the claim on summary judgment, on the basis that the antitrust laws impose no such duty. Florida Cities v. Florida Power & Light Co., 525 F. Supp. 1000 (S.D. Fla. 1981), vacated as moot, No. 79-5101-Civ-JLK (March 23, 1982).

49/ APCO's offer showed a price for the total plant of $2,697,524,000. Franklin Affidavit, Attachment 4. The nameplate capability of the two units is 1720 kw. $2,697,524,000 divided by 1720 kw equals $1568/kw. These
(footnote continued)

the offer at pp. 17-22 of his affidavit. Essentially, APCO commissioned EBASCO Services, Inc. to perform a study of the cost of replacing Plant Farley with a nuclear generating plant of similar size and age that was postulated to enter service in July 1983. 50/ APCO also estimated a price based on its total costs associated with Plant Farley. The two resulting figures were averaged to obtain the sale price offered to AEC. 51/ The offer was presented to AEC as a negotiating position that is subject to compromise. 52/

We demonstrate below that: (1) APCO's offer is below the fair market value of Plant Farley, a plant that has established a record of extremely reliable operation as compared with other commercial nuclear power plants in the United States; and (2) the considerations taken into account in APCO's estimate of its costs related to Plant Farley are appropriate for determination of a price sufficient for recovery of a proportionate share of APCO's total costs, including "an adequate return on [its] earlier investment, predicated upon the risk elements which it involved". 53/ Thus, under any reasonable interpretation of the License Condition, APCO's position on the sale price issue

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(footnote continued from previous page)
numbers do not include nuclear fuel, and are calculated for a sale as of June 30, 1983.

50/ Franklin Affidavit, p. 22.

51/ Id., p. 18.

52/ Id., p. 27.

53/ Sullivan, supra, Handbook of the Law of Antitrust, p. 132.

reflects good faith compliance with the terms of its NRC license.

a. The Fair Market Value of Plant Farley Exceeds the Sales Price that APCO Has Offered to Accept

For the reasons explained above, in section III, B, 2, and in the attached Affidavit of Dr. Charles Cicchetti, the appropriate standard by which APCO's offer should be measured is that of commercial reasonableness, or fair market value. 54/ Is a sale price of $1568 per kw for a nuclear power plant with an excellent and established operating record out of line with the price that would be sought by a willing seller in a market free of artifical restraints?

The answer is very clear. As Dr. Cicchetti explains, a rational seller in a commercial transaction seeks to recover its opportunity cost. 55/ A conservative measure of opportunity cost where, as here, the seller has a long term need for nuclear generating capacity, is the cost that the seller would incur in replacing the capacity sold to AEC. EBASCO estimated APCO's replacement cost to be $1724 per kw. 56/ Clearly, the EBASCO study provides an extremely conservative measure of APCO's replacement cost. It was predicated on the overly conservative assumption that the replacement facility would enter service in

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54/ Cicchetti Affidavit, p. 3.

55/ Cicchetti Affidavit, p. 10.

56/ Franklin Affidavit, p. 22. The $1724 per kw figure is obtained by dividing the total replacement cost figure of $2,965,000,000 found at p. 1 of the EBASCO study, by the nameplate capability number of 1720 kw, likewise found at p. 1 of the study. These numbers do not include nuclear fuel. Id., Attachment 5.

1983. Moreover, it simply quantifies the increase in cost of materials and services that would have been experienced had a nuclear unit similar to one of the Plant Farley units been constructed between 1971 and 1983. Any observer of the nuclear power industry can attest that, for anyone beginning construction of a nuclear power plant in 1971, other factors extraneous to the cost of materials and labor have exerted upward pressure on costs. These factors include rapidly evolving regulatory requirements, particularly in the wake of the Three Mile Island incident, and public acceptance problems that have manifested themselves, among other ways, in lengthy and contested licensing proceedings. 57/ Dr. Cicchetti illustrates these facts with his comparison of the replacement cost estimated by EBASCO with the current cost estimate of several nuclear power plants which were constructed during the 1970's. 58/

APCO's offer is $1568 per kw, well below EBASCO's eplacement cost estimate of $1724 per kw. By any standard, this is a bargain price for units with the superb operating records of the Plant Farley units. 59/ It is below the price that a willing seller in any ordinary commercial transaction could be expected to accept. 60/

57/ Id., p. 23.

58/ Cicchetti Affidavit, pp. 11-12.

59/ Franklin Affidavit, p. 24.

60/ Cicchetti Affidavit, p. 12.

b. APCO's Offer Properly Recognizes That Recovery Of A Proportionate Share Of APCO's Total Costs Is Dependent On Making Certain Adjustments To Public Utility Accounting Costs, And On Providing For Recovery Of Risk Related Costs

Not only is the sale price proposed by APCO less than the fair market value of the interest offered to AEC, it also incorporates principles essential to determination of APCO's true original cost, less depreciation, of that portion of the Farley Plant offered to AEC. APCO's original costs consist of two classes of components: (1) those costs that can be identified from examination of APCO's accounts ("accounting costs"), and (2) costs associated with risks borne by APCO in designing and constructing Plant Farley, which can be estimated but not calculated with mathematical precision.

Why is it not possible to determine APCO's total original cost of Plant Farley by doing nothing more than looking at the entries on APCO's books for Plant Farley? The problem is that the accounts maintained by APCO, in accordance with regulations of the FERC and the Alabama Public Service Commission ("APSC"), are designed to serve the requirements of utility ratemaking. Utility rates are determined by viewing the utility's total production plant, and related expenses, as a composite whole and developing percentage allocation factors to allocate responsibility for total production costs among classes of customers. Since each class of customer is responsible for the same per-

centage of costs associated with each generating plant, there is no need for differentiating between, for example, the costs of capital used during construction of a plant completed in 1955 and one completed in 1981. The accounting procedures prescribed by the FERC and the APSC were not designed to determine the appropriate sale price for a facility such as Plant Farley. 61/ This is evidenced by Section 203 of the Federal Power Act, requiring explicit FERC approval of the terms of sale of facilities subject to the FERC's jurisdiction, although this jurisdiction does not extend to generating plants. 62/

(1) Accounting costs

The beginning point for a calculation of accounting costs is the amount expended by APCO for materials and services for design, licensing and construction of Plant Farley. There appears to be no dispute that the figures recorded on APCO's accounts correctly describe the costs of these items. There are two other categories of accounting cost: (i) allowance for funds used during construction ("AFUDC") and (ii) cost associated with tax liabilities.

APCO recorded AFUDC on its books in accordance with procedures prescribed by the FERC. Under the regulatory standards that prevailed while Plant Farley was under construction, a

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61/ This is explained in more detail in the Walker Affidavit, pp. 7-8.

62/ 16 U.S.C. § 824b. Transmission facilities, but not generation facilities, are subject to the FERC's jurisdiction. FPA, § 201, 16 U.S.C. § 824(b).

utility is not permitted to earn a return on property until construction has been completed and the facility is used to provide service to customers. However, during the years while construction is in progress, capital must be devoted to construction. The utility must pay a cost for capital, and regulators recognize that the utility is entitled to recover this cost.

AFUDC is the accounting technique used to provide for this cost recovery, on a basis that is consistent with the regulatory policy of deferring any return associated with a plant until that plant enters service. The utility records AFUDC on its books during construction. Upon commercial operation of the facility, the accumulated AFUDC is treated as a part of the cost of the plant, just as the cost of materials and labor used for construction. This total cost then becomes part of the utility's "rate base" for ratemaking purposes. The utility recovers the total amount of its rate base, over time, through allowances for depreciation that are recognized or expenses recoverable through rates. It also recovers an annual return on the undepreciated portion of its rate base, based on the rate of return allowed by regulation.

Although the formula for calculating AFUDC is complex, 63/ the cost of capital incorporated in the formula consists of four

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63/ 18 C.F.R. Part 101 Uniform System of Accounts Prescribed for Public Utilities and Licensees Subject to the Provisions of the Federal Power Act (Class A and B), Electric Plant Instructions (17).

components: (i) short term debt, (ii) long term debt, (iii) preferred stock, and (iv) common equity. No adjustment is required to the cost of short term debt used in APCO's initial calculation of AFUDC. In calculating the AFUDC rate, APCO used its average embedded cost of total debt and preferred stock outstanding at any given time. Thus, as noted by Mr. Walker in his affidavit, if at the end of 1980 APCO had two series of bonds outstanding--a $1,000,000 series issued in 1955 calling for an interest rate of 5% and a $1,000,000 series issued in 1979 calling for an interest rate of 15%--the cost of debt used in the AFUDC formula would be based on the weighted average of the two, or 10%. Obviously, this understates the cost of money that was borrowed, in 1979, to finance construction expenditures made in 1979. The FERC has recognized that when a utility sells power from a designated new unit ("unit power"), the interest and dividend rates provided in bonds and preferred stock actually issued during the construction period should be used to determine the cost of capital. 64/ Mr. Walker testifies that similar principles should be applied in this case. 65/ Indeed, if such principles were not applied APCO would clearly not recover the cost of capital actually used for construction of Plant Farley.

64/ Connecticut Light & Power Company, FPC Opinion No. 701, 52 FPC 175 (1974).

65/ Walker Affidavit, pp. 13-14.

FERC rules provide that AFUDC may be "compounded" twice each year, in the same manner that interest on a savings account is applied to the entire balance of the account, including interest previously earned and credited. 66/ The AFUDC shown on APCO's books does not fully reflect this compounding effect. Mr. Walker testifies that it is appropriate to make an adjustment to the AFUDC recorded on APCO's books to reflect fully application of the FERC compounding rule. Clearly, it costs as much to attract capital that is used to pay the carrying cost of capital already committed to a project as it does to attract capital that is used to buy materials and pay construction workers; all of these expenditures are part of APCO's total costs related to Plant Farley. 67/

The final category of adjustments recognized by Mr. Walker concerns the taxes that APCO will be required to pay following the sale. With one exception noted below, these tax effects are all associated with AFUDC, which is based on the concept of deferring APCO's return on the capital tied up during construction of Plant Farley until the plant entered service.

The AFUDC concept is a ratemaking concept. On the other hand, APCO's tax liabilities are determined by tax laws, which permit expenses to be deducted when they are incurred and subject income to taxation when it is received. AFUDC is part of the cost of a generating facility recognized for utility accounting

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66/ Id., p. 14.

67/ Id., pp. 14-15.

and ratemaking purposes, but is not included in the tax basis of the facility. In accordance with utility accounting procedures, APCO treated the AFUDC recorded during construction of Plant Farley as "after-tax income", although none of that income was recovered or taxed prior to commercial operation of the units. Likewise, although APCO could not wait until commercial operation of the units to pay interest on money borrowed to construct them, APCO was not permitted to recover any of this cost from its ratepayers until after commercial operation. Yet, interest payments were deducted for tax purposes at the time they were actually made.

The critical points are: (1) APCO must recover the AFUDC properly attributable to Plant Farley if it is to recover the cost of capital that it actually incurred during construction. (2) Under the rules of the FERC and the Alabama Public Service Commission, the capital cost rates used in calculating AFUDC are "after tax" rates; that is, they reflect the return on each component of the capital structure that the utility is entitled to have left over after all tax expenses have been met. (3) The taxes identified in Mr. Walker's affidavit must actually be paid by APCO from the proceeds of the sale to AEC. Therefore, if APCO does not recover a sales price that is sufficient to discharge these tax liabilities and leave APCO with the AFUDC which is properly includable in its total costs of the portion of

Plant Farley sold to AEC, APCO will not have recovered a proportionate share of its total costs and will have been forced to sell to AEC at a loss.

With this background, we turn to the specific components of the tax adjustment discussed by Mr. Walker.

(A) Restoration of Reduction in Booked AFUDC Resulting From Deferred Taxes Associated With Debt Portion of AFUDC. As explained above, during construction of the Plant Farley APCO was required to pay interest on money borrowed to finance construction, but was forced to defer collection of this cost from its ratepayers. APCO was able, however, to deduct interest payments at the time they were actually made and thus reduce its tax liability currently payable for each year during the construction period. An equal and offsetting provision for deferred taxes was made for accounting and ratemaking purposes. Since APCO did not receive the income required as reimbursement for its interest cost until after the year in which deductions for interest payments were taken, an additional tax, equivalent to the initial tax deferral, must be paid at the time when the income is received. Thus the reduction in taxes currently payable was not a "tax savings" but merely a deferral of taxes payable. In the interim, APCO has the use of the money. However, regulators require that these deferred taxes be used for the benefit of customers, and therefore they reduce (or offset) a utility's "rate base" (the investment on which it is permitted to earn a return) by the amount of accumulated deferred taxes.

There are two accounting methods for achieving this "offset against rate base" effect. The first is the "net-of-tax" method, under which the utility reduces the amount of AFUDC that it records by the amount of taxes deferred, thus reducing the amount of AFUDC that is placed in the rate base upon commercial operation of the facility. The second is the "gross-of-tax" method, which permits a utility to record the full amount of AFUDC and to create a separate deferred tax account which will be offset against its rate base in determining rates. The "net-of-tax" method was used by APCO. Both methods have exactly the same effect on ratepayers. Moreover, these accounting techniques have no relationship to the actual cost of a plant.

Where a portion of a plant is removed from the rate base and sold, the net-of-tax accounting method clearly understates the AFUDC that should be included in the seller's total costs. The AFUDC recorded on APCO's books should be adjusted to eliminate the offset effect attributable to deferred taxes -- taxes which will no longer be deferred following consummation of the sale (as regards the proportion sold). Mr. Walker explains this adjustment in his affidavit under the heading "Item 1".

A related principle applies to the amounts discussed in Mr. Walker's affidavit under "Item 4". This adjustment is not related to AFUDC, but to other deferred tax items. Certain taxes, related to items other than interest costs, were effectively deferred during the construction process or as a result of accelerated depreciation reductions taken by APCO after

commercial operation of Plant Farley and passed along to ratepayers in the form of lower rates. For example, some costs that were capitalized under utility accounting principles were deducted as expenses for tax purposes at the time they were incurred, e.g., some construction overhead costs. In effect, the period of deferral of such tax obligations ends with the sale. These taxes are properly includable in APCO's costs.

(B) Income Taxes Necessary to Recover Preferred and Common Equity Portions of AFUDC. The AFUDC portion of APCO's investment in Plant Farley also includes provisions for return on common and preferred stock capital used for construction of Plant Farley. This portion of AFUDC is part of APCO's cost of constructing Plant Farley and APCO must receive sale proceeds sufficient to pay these taxes in order to recover its AFUDC on an "after tax" basis. Absent a sale to AEC, APCO would recover this amount, plus an annual return on the undepreciated amount of AFUDC, ratably over the estimated life of the Plant Farley units. 68/

68/ Following the sale, AEC will likewise recover both the principal amount of the sale price and an annual return on the undepreciated balance from its customers over the remaining life of Plant Farley. The difference is that the return will be at the lower, subsidized cost of capital available to AEC and that, because it does not pay taxes, AEC will not need to recover any tax expenses through its rates. Thus, by buying now, AEC avoids paying the amounts, including tax expenses, associated with permitting APCO to earn a continuing return on the undepreciated balance of AFUDC. Whether or not a sale is made, a tax liability is associated with APCO's recovery of costs of equity capital incurred while, from 1972 until 1981, that capital was tied up in construction of Plant Farley.

The calculation of tax liability depends on the allocation of the taxable gain between capital gain and ordinary income, an allocation that is exceedingly complex. Accordingly, if the sale price were to be based upon a cost calculation, as contrasted with fair market value, it would be appropriate to provide for a "true up" so that AEC would pay, in respect of taxes, an amount equal to the tax liability that is actually incurred by APCO after its tax returns have been submitted to and reviewed by federal and state revenue agencies.

In concluding the discussion of accounting costs, it is important to reemphasize that the adjustments discussed in Mr. Walker's affidavit involve real costs that are, beyond any doubt, attributable to Plant Farley. If APCO were to be required to sell an interest in Plant Farley at a price that is below the level required to reflect each of these items APCO would not recover even its accounting costs, much less other economic costs, related to Plant Farley.

(2) Risk

As a matter of sound economics and equity, the cost of funds used during construction of Plant Farley should include a return on common equity ("ROE") that compensates APCO for risks that it took and that AEC did not share, i.e., the risks that Plant Farley would not be licensed and completed and/or would not operate reliably and dependably. Dr. Cicchetti's affidavit illustrates that these risks were real indeed. Two other plants

that received construction permits in the same time frame that the Plant Farley permits were issued, Consumers Power Company's Midland Plant and Cincinnati Gas and Electric Company's Zimmer Plant, were each cancelled after more than a billion dollars had been invested in design and construction. These stark facts emphasize the absurdity of AEC's claim that, even though it bore none of these risks, it should be permitted to purchase an ownership interest at a price that takes no account of the actual costs and risks borne by APCO and its shareholders up to the sale date.

The ROE's used to calculate the AFUDC recorded on APCO's books for Plant Farley reflect the ROEs allowed, from time to time, by state regulation in Alabama for APCO's total utility operations. There can be no doubt that Plant Farley was by far the most risky venture in which APCO was involved during the 1972-1981 period, and would alone have required a much higher ROE. Moreover, the overall ROE allowed to APCO during much of this period, particularly 1973 through 1981, was not sufficient to prevent financial hardship for APCO, its parent the Southern Company, and the Southern Company's shareholders. The new shares of Southern Company common stock, issued to finance construction of Plant Farley, were consistently marketed below book value and diluted the book value of existing shares. 69/

69/ Franklin Affidavt, pp. 20-21; Cicchetti Affidavit, p. 14.

Therefore, it is abundantly clear that the ROEs contained in AFUDC booked for Plant Farley are too low to compensate APCO fairly, in the event of a sale of an interest in Plant Farley, for the risk borne by APCO in bringing the project to its current, highly successful status. If, contrary to its view of the License Condition, APCO were required to sell an interest in Plant Farley at a price based on a some calculation of costs, an adjustment to reflect this risk factor would be essential.

C. APCO's Negotiating Position on the Issue of Percentage Ownership Share is Consistent With the License Condition

The disagreement over the percent ownership interest required to be conveyed also appears to reflect posturing by AEC designed to prolong the negotiations. The License Condition unambiguously bases the formula for determining the percentage to be sold on "the respective peak loads of AEC and the Licensee." As explained in the affidavit of Mr. Franklin, 70/ AEC has taken the position in negotiations that wholesale power sales made by SEPA to AEC's "off-system" members should be included in AEC's peak load for the purpose of the calculation. This position just does not conform to the clear language of the License Condition, and APCO has therefore been unwilling to treat power supplied by SEPA as loads of AEC to be considered in determining AEC's peak load. It is this conflict which accounts for the difference between APCO's offer to sell a 6.26% interest and AEC's demand that APCO transfer 6.7% of the plant to AEC.

70/ Franklin Affidavit, p. 33.

AEC's position would deny that SEPA has any wholesale load responsibility in Alabama, since it effectively treats all loads served by SEPA as being loads of other parties. This is inconsistent with the analysis of the Department of Justice witness Wein, whose testimony on market shares, discussed in the Licensing Board's decision at 5 NRC 881, shows SEPA having a 2% share of the wholesale market in Central and Southern Alabama. Indeed, throughout the entire proceeding, the SEPA loads were recognized as loads of SEPA, not loads of AEC or APCO.

Moreover, AEC's position is inconsistent with the position which it has taken only recently in connection with treatment of SEPA's sales to AEC's off-system customers on whose behalf APCO wheels AEC's power. In correspondence between APCO and AEC, AEC was given the option by APCO of having this load treated as a load of AEC or a load of SEPA. AEC unambiguously chose to have it treated as a SEPA load. 71/

The difference between the percentage share offered by APCO (6.27%) and AEC's position (6.7%) amounts to approximately 7.4 megawatts of name plate capacity. At a time when the cost of replacement capacity exceeds $2000 per kilowatt, it should be recognized that the retail customers of APCO have a great deal at stake - particularly since AEC is not proposing to pay replacement cost for such capacity. During the arguments before the Eleventh Circuit, the attorney representing the NRC and the Department of Justice stated that the Appeal Board's order would

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71/ Id., Attachment 8.

result in a sale of only 4 - 6% of the plant. That representation was apparently relied on by the Eleventh Circuit. Nevertheless, AEC purposefully misreads the License Condition to demand a 6.7% interest in the plant.

D. APCO's Negotiating Position on the Other Issues Raised by AEC is Responsible and Commercially Reasonable

The License Condition is silent with respect to a number of terms and conditions that might appropriately be included in a contract for the sale of an ownership interest in a facility such as Plant Farley. For example, the condition does not suggest the content of provisions relating to apportionment of liability between APCO and AEC, and does not deal with the subject of the manner and security of payment by AEC for its share of capital and operating costs. Since these matters must clearly be resolved through good faith negotiations between the parties, the applicable standard for measuring APCO's compliance with the License Condition, where such issues are concerned, is simply whether the terms proposed by APCO are consistent with good business practice and are not, as AEC asserts, "plainly unreasonable." 72/ AEC invokes this commercial standard when it characterizes conditions in APCO's offer as "unreasonable" and "unconscionable". 73/ In fact, as will be shown below, APCO's

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72/ AEC Enforcement Action Request, p. 10.

73/ Id., p. 9.

position on each of the issues listed by AEC 74/ is commercially reasonable and justified by legitimate business considerations.

1. APCO's Security Proposals Represent Exercise of Normal, Prudent Business Judgment

As a co-owner of Plant Farley, AEC would be responsible for a proportionate share of the costs of operating, maintaining and improving the facility. Payment of these expenses would normally be consistent with AEC's own interest in protecting its investment in Plant Farley and in averting default under the purchase and operating agreements. However, substantial amounts may be due under these agreements in circumstances where Plant Farley is no longer an economic asset. This is the case with respect to decommissioning the plant at the end of its productive life, which will involve costs that cannot be accurately determined in advance, and the expenditure of which will not directly benefit the owners. It is also true in the event of an occurrence such as the incident that took place at the Three Mile Island Nuclear Plant, which resulted in uninsured costs in excess of $1,000,000,000 75/ and the likelihood that the affected unit will never be utilized.

A minority owner's motivation to pay these costs, at a time when future production from the plant cannot be expected as the reward, may depend on the extent to which avoidance of its financial obligations is economically feasible. In APCO's own

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74/ Id., pp. 9-10.

75/ Kron Affidavit, p. 2.

case, as Mr. Kron observes, an equity investment in excess of $1,500,000,000 stands behind its performance. 76/ A firm with less at stake might, however, be more tempted to avoid its decommissioning and clean-up obligations.

Considerations such as these led APCO to seek reasonable assurance that AEC will pay its share of all expenses which arise. Analysis of AEC's recent financial statements reveals that AEC's property is subject to an REA mortgage equivalent to the net cost of its assets and creating a first lien on all its revenues, 77/ and that, in contrast to APCO's strong financial position, it has a "negative equity", 78/ its balance sheets reflecting liabilities in excess of assets.

The concern that these facts caused APCO was reinforced by its understanding of AEC's corporate structure. AEC, a generating and transmission cooperative, is, in effect, a subsidiary wholly owned and controlled by its member distribution cooperatives, which provide AEC's only source of revenue by purchasing their energy requirements from AEC under 45 year power supply contracts. 79/ AEC's customers/owners will thus be able t maintain AEC in a negative equity position and even, if

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76/ Id., p. 3.

77/ Id.

78/ Franklin Affidavit, p. 35.

79/ The term of these contracts is far shorter than the period during which decommissioning costs may be incurred, such that even if AEC were able to enforce its agreements with its parent members these could terminate long before AEC's obligations to APCO.

economically advantageous, to dissolve AEC in bankruptcy proceedings and to replace AEC with another power supply subsidiary free of the Farley Plant commitments. AEC's answer to these concerns is that it should be trusted to act responsibly and to refrain from legal maneuvers designed to avoid compliance with the spirit of its obligations. However, in light of the actions that have been taken by municipal and cooperative utilities in the Pacific Northwest to avoid meeting similar commitments regarding the WPPSS nuclear generating units, APCO cannot prudently rely upon the assurance of AEC's current managers and directors, who are unlikely, in any event, to remain in office through the entire term of the Plant Farley agreements.

As Mr. Kron testifies, under the circumstances, and in light of APCO's continuing responsibility as an NRC licensee for the full costs of any necessary clean-up or decommissioning, attempts by APCO to reduce the risk that it will be unable to recover from AEC the latter's proportionate share of the expenditures conform to normal, prudent business practice. 80/ APCO submitted for AEC's consideration several different security arrangements that, alone or in combination, might accomplish this purpose, including: a guarantee by REA of AEC's performance; a grant by AEC to APCO of a second mortgage, behind REA, on AEC's facilities; advance funding by AEC; 81/ and a guarantee by its members of

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80/ Kron Affidavit, p. 3.

81/ This proposal does not appear in APCO's most recent offer. Funding of decommissioning and disposal costs is, however, (footnote continued)

AEC's full satisfaction of its obligations. Contrary to AEC's assertion, 82/ APCO has not demanded that all of these proposals be accepted as a condition to the sale. APCO's negotiating position has been, rather, that some appropriate provision or combination of provisions must be made to forestall its having to pay costs AEC is contractually obliged to cover, and that the various security provisions it has suggested accord with prudent and reasonable business practice.

This claim is supported by Mr. Kron. Mr. Kron testifies, in particular, that the option of obtaining a payment guarantee by AEC's member cooperatives is a highly desirable one. 83/ Indeed, the standard commercial approach taken by a firm contracting with a subsidiary having little or no net worth is to engage the commitment of its more credit worthy parents. This is especially appropriate in this case, where AEC's "parents" are both the direct economic beneficiaries of AEC's participation in Plant Farley and AEC's sole revenue source. AEC's members have access to a stream of revenue from their customers, who rely on them for service and are the ultimate beneficiaries of the agreements between APCO and AEC. AEC's members cannot be harmed by formally guaranteeing payment of obligations that they assert they are already bound by their power supply contracts with AEC to meet

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(footnote continued from previous page)
consistent with FERC practice where a power supply company is involved.

82/ AEC Enforcement Action Request, pp. 9-10.

83/ Kron Affidavit, p. 4.

in any event. APCO's request that AEC's members provide such security thus meets the standard of commercial reasonableness contemplated in the license condition.

2. The Liability and Indemnity Clauses Proposed by APCO Are Commercially Reasonable

The license condition contemplates that APCO will continue to conduct "the day-to-day operation of the plant," and permits APCO to condition its offer to sell an ownership interest on AEC's agreement not to interfere. A high degree of managerial experience and competence is essential to proper operation of a facility such as Plant Farley. The requisite management skills are certainly of significant economic value; APCO is nonetheless willing to make these available to AEC on a basis that is intended merely to compensate APCO for AEC's proportionate share of the true costs of operating Plant Farley. In such circumstances, a disclaimer of liability for claims that do not result from willful misconduct is in fact common practice where joint ownership of nuclear projects is concerned. 84/

AEC contends that it is "unconscionable" for APCO to limit its liability to AEC for the consequences of operating decisions and to insist that AEC be responsible for a proportionate share of any fines or penalties assessed against the owners of the

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84/ Other participation agreements for nuclear generating plants that contain similar provisions include agreements pertaining to the St. Lucie, Pilgrim, South Texas and Clinton Plants.

plant. 85/ AEC also complains that "APCO refuses to make even the barest commitment to operate the Farley Plant in a reasonable manner." 86/ The implication that AEC's agreement to contribute its proportionate share to the payment of any damages or fines may encourage APCO to ignore its obligations to the NRC as licensee of a nuclear generating facility and to its shareholders and customers to conduct its operations in a prudent and reasonable manner is absurd. The best evidence of APCO's commitment to operate Plant Farley reasonably and conscientiously is the $1.5 billion equity investment of APCO's shareholders that is at risk with respect to APCO's 94% interest in Plant Farley. APCO asks only that AEC assume its proportionate share of all costs that result from mistakes that were not intentional on the part of APCO's management. AEC desires to share in the benefits of APCO's successful operation of Plant Farley but to shirk the attendant risks.

AEC's apparent wish that APCO not only bear AEC's share of the risk of third party liability, but also assume liability to AEC, is outrageous. AEC expects APCO to assume sole operating responsibilities on a non-profit basis, while remaining fully liable to AEC for unintentional as well as willful conduct, and,

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85/ AEC Enforcement Action Request, p. 10. AEC erroneously asserts that APCO seeks to hold AEC liable for penalties relating to conduct which occurred prior to AEC's ownership participation. APCO does not take such a position.

86/ Id.

moreover, seeks to avoid its proportionate share of responsibilities to third parties. The License Condition clearly does not require that APCO agree to such an unreasonable demand.

3. APCO's Negotiating Position With Respect to Regulatory Approvals is Taken in Good Faith and Is Commercially Reasonable

AEC also complains about what it describes as APCO's refusal "to agree in any way to assist in the gaining of necessary regulatory approvals for AEC's acquisition of its ownership share" of Plant Farley. 87/ Such a characterization of APCO's position is not at all accurate. APCO's position on this issue was stated by APCO Executive Vice President Jesse Vogtle in a letter dated September 26, 1983, to Charles Lowman, Manager of AEC, as follows:

> "APCO is willing to assure AEC that it will furnish AEC any information which APCO has that is needed for AEC to process any application for necessary approvals. APCO is unwilling to commit that it will forego any right or duty that it may have to object to the approval. It will make any formal application to NRC that may be required for NRC to determine whether AEC should become a licensee, however, in so doing it shall not waive its right to comment as it sees fit during the approval process." 88/

AEC makes no effort to explain why APCO's unwillingness to muzzle its right to express its own views and to come forth with information that AEC may wish withheld from governmental agencies is unreasonable. The "gag rule" sought here to be imposed by AEC

87/ AEC Enforcement Action Request, p. 10.

88/ Franklin Affidavit, Attachment 9.

is not an ordinary condition to a commercial contract, and would require APCO to act in ways contrary to the candid behavior normally expected of parties offering information to regulatory bodies. APCO's stated intention to provide any material in its possession required by any government agency to evaluate AEC's applications, without agreeing to limit its participation in the approval process to accord with AEC's demands, is both commercially reasonable and appropriate in the context of the regulatory process.

4. APCO's Negotiating Position with Respect to Incremental and Not Precisely Quantifiable Costs is Commercially Reasonable and Consistent with the Spirit of the License Condition

As the discussion in III, B, above, demonstrates, the license condition is not a penalty and does not contemplate that APCO will in any sense subsidize AEC's acquisition of an ownership interest in Plant Farley. 89/ At minimum, APCO is entitled to recover in the sales price a pro rata share of its total actual costs as of the date of sale. This principle applies with even greater force with respect to costs that will be incurred upon or following the sale, and necessitates that the continuing

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89/ The antitrust laws do not require even a monopolist "to affirmatively assist potential competitors by subsidizing their entry into the marketplace or granting them preferential access to a unique facility." Town of Massena v. Niagara Mohawk Power Corp., 1980-2 Trade Cas. (CCH) ¶ 63, 526, at p. 76, 814 (N.D.N.Y. 1980).

expenses of owning, operating and modifying the plant be shared by the owners in proportion to their interests. APCO's offer is based on this understanding, which is not challenged by AEC.

In its Enforcement Action Request, AEC criticizes two applications of this basic approach. In particular, AEC objects to APCO's proposals that AEC be responsible for incremental costs experienced solely as a result of the sale, 90/ and that AEC pay certain fees associated with APCO's costs of operating, maintaining, improving, and acquiring nuclear fuel for the facility. 91/

It is apparent, however, that APCO's position on these issues is reasonable and in accord with the underlying intent of the license condition, and that AEC's complaints are unjustified. APCO's most recent offer requires AEC to pay "incremental costs experienced by APCO solely as a result of the sale to AEC of an ownership interest in the Farley Plant including, but not limited to: (a) the adverse impact on APCO of any tax legislation, or interpretation of tax laws; (b) special accounting requirements; (c) requirements of REA, or other governmental agency, which APCO would not have incurred but for AEC's participation." 92/ An example of such costs concerns the "Buy American" clause that, according to AEC, must be contained in any contract executed by a cooperative that intends to utilize a financing subsidy from the

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90/ AEC Enforcement Action Request, p. 10.

91/ Id., pp. 4-5.

92/ Franklin Affidavit, Attachment 10, p. 16.

REA. If compliance with this provision increases the costs of materials for a capital improvement to Plant Farley, AEC, the beneficiary of the REA subsidy, should bear all of these costs. Certainly, they should not fall upon APCO's customers. APCO's objective is to preclude the possibility that it will be liable to pay the lion's share of expenses that represent, in effect, costs of AEC's entry, rather than project costs. Assumption of such an obligation equates to a subsidy of AEC's participation, and is clearly not the sort of commitment a prudent businessman would make.

APCO's position on the operating expense issue is also commercially reasonable. As Mr. Franklin testifies, successful operation of a nuclear project is a costly, valuable service. 93/ APCO recognized that its accounting system does not capture completely the total costs associated with the plant's operation, particularly the cost of management attention paid specifically to the facility. 94/ As the Director is acutely aware, the NRC demands that the operation of nuclear power plants receive an extraordinary level of "hands on" attention by management. APCO complies fully with the spirit of this policy. APCO's most recent proposal therefore includes an assessment against AEC of an additional 10% of its pro rata share of the operating and maintenance expenses to cover costs to APCO that are not susceptible to precise quantification. Whether this assessment

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93/ Id., p. 41-42.

94/ Id., pp. 42-43.

is referred to as an operating fee, 95/ or as an allowance for unquantifiable costs, it is less than amounts routinely allowed by FERC for such costs, 96/ and represents a reasonable and prudent attempt to reduce the likelihood that AEC will avoid its proportionate cost responsibility.

IV. CONCLUSION

It is clear for the reasons stated above that APCO's offer was presented in good faith and complies with the standards of the License Condition. Therefore AEC's Enforcement Action Request should be denied.

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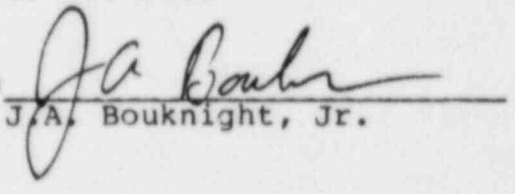
By: 
J.A. Bouknight, Jr.

October 15, 1984

95/ See AEC Enforcement Action Request, p. 5.

96/ Franklin Affidavit, p. 43.

UNITED STATES OF AMERICA
NUCLEAR REGULATORY COMMISSION

Before the Commission

In the Matter of	)	
ALABAMA POWER COMPANY	)	Operating Licenses
(Joseph M. Farley Nuclear Plant	)	
Units 1 and 2)	)	Nos. NPF-2 and NPF-8
	)	

PETITION OF ALABAMA
POWER COMPANY FOR A
DECLARATORY ORDER

Alabama Power Company ("APCO") respectfully requests that the Commission institute proceedings leading to the issuance of a declaratory order clarifying APCO's obligations under antitrust condition number 2.F.(2) contained in APCO's Operating Licenses Nos. NPF-2 and NPF-8, as such licenses were amended on August 10, 1981. ("License Condition"). The License Condition, imposed following the antitrust review which was conducted pursuant to Section 105c of the Atomic Energy Act, requires APCO to offer to sell to Alabama Electric Cooperative, Inc. ("AEC") an ownership interest in the Joseph M. Farley Nuclear Plant, Units 1 and 2 ("Farley Plant"), at a price to "be established by the parties through good faith negotiations" which "will fairly reimburse Licensee for the proportionate share of its total costs ...including, but not limited to, all costs of construction, installation, ownership and licensing ...."

APCO makes this request because APCO and AEC have differing opinions concerning the proper interpretation of the License Condition and have been unable to agree on the essential terms of the sale of the ownership interest in the Farley Plant. A declaratory order issued by the Commission would be the most efficient and expeditious means of resolving the differences.

The Commission clearly has the authority to render a declaratory order, and declaratory relief is particularly appropriate in this instance. The original antitrust proceeding before the Commission lasted over 9 years, involved 170 days of hearings, and culminated in a 157 page initial decision and an 87 page Appeal Board decision. Judicial review added another 3 years to the process. In fairness to the parties and in the interest of administrative efficiency and economy, this issue should be resolved as expeditiously as possible by the Commission itself without setting in motion still another round of adjudicatory hearings that would prolong the uncertainty over the ownership interests in the Farley Plant and divert the valuable time and resources of the NRC Staff and the other parties from other, more pressing tasks. Moreover, the issues presented involve important policy questions that can, and should, be resolved by the Commission. As demonstrated below, the procedures here suggested would make it possible for the Commission to resolve those questions without instituting burdensome and lengthy administrative proceedings and without unduly involving itself in matters of detail.

In further support of its petition, APCO submits the following:

I. Need for a Declaratory Order

The License Condition was imposed by the Atomic Safety and Licensing Appeal Board ("Appeal Board") in its order dated June 30, 1981, 1/ and was incorporated in amendments to the operating licenses for the Farley Plant issued on August 10, 1981. In pertinent part, it reads:

> 2. Licensee shall offer to sell to AEC an undivided ownership interest in Units 1 and 2 of the Farley Nuclear Plant. The percentage of ownership interest to be so offered shall be an amount based on the relative sizes of the respective peak loads of AEC and the Licensee (excluding from the Licensee's peak load that amount imposed by members of AEC upon the electric system of the Licensee) occurring in 1976. The price to be paid by AEC for its proportionate share of Units 1 and 2, determined in accordance with the foregoing formula, will be established by the parties through good faith negotiations. The price shall be sufficient to fairly reimbuse Licensee for the proportionate share of its total costs related to the Units 1 and 2 including, but not limited to, all costs of construction, installation, ownership and licensing, as of a date, to be agreed to by the two parties, which fairly accommodates both their respective interests. The offer by Licensee to sell an undivided ownership interest in Units 1 and 2 may be conditioned at Licensee's option on the agreement by AEC to waive any right

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1/ Alabama Power Company (Joseph M. Farley Nuclear Plant Units 1 and 2), ALAB-646, 13 NRC 1027 (1981), aff'd, Alabama Power Company v. Nuclear Regulatory Commission, 692 F.2d 1362 (11th Cir. 1982), cert. denied, 104 S.Ct. 72 (1984).

of partition of the Farley plant and to avoid interference in the day-to-day operation of the plant.

Soon after the Appeal Board Order became effective, APCO began to provide information for AEC's review. AEC indicated a desire to review a substantial amount of financial and other data before commencing substantive negotiations over acquisition of an interest in the Farley Plant. 2/ In March 1983, AEC indicated that it was prepared to proceed with negotiations, and in April 1983 APCO communicated its initial offer to sell an interest in the plant to AEC. (See Appendix 7). Negotiations have continued until the present, 3/ and Appendices 10, 11 and 12 are copies of the Purchase and Ownership Agreement, the Operating Agreement, and the Nuclear Fuel Agreement that comprise APCO's current offer to AEC. These negotiations have failed to resolve several fundamental issues as to the interpretation of the License Condition.

While the parties to the negotiations undoubtedly hold different perceptions concerning the reasons for this disagreement, it is primarily due to conflicting interpretations of the broad, general terms of the License Condition. It is APCO's position that AEC has exhibited a persistent unwillingness to compromise on a number of critical issues set forth in the

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2/ See Appendices 5 and 6. Appendices 1 through 4 reflect AEC's requests for, and APCO's provision of, data for review by AEC's consultants.

3/ See Appendices 8 and 9, summarizing the positions of the parties in the fall of 1983. More recently, the parties' exchange of positions is reflected in Appendices 13 and 14.

agreements that were to be "established by the parties through good faith negotiations" and on a basis that "fairly accommodates both their respective interests." (Some of these issues are described in greater detail in Section III, below.) In any event, further negotiations between the parties do not seem likely to resolve the differences.

As a result of the dispute over interpretation of the License Condition, APCO remains obligated to comply with the License Condition and yet faces uncertainty as to when and whether AEC will ever actually purchase an ownership interest. This uncertainty leads to an unfair situation in which APCO continues to be responsible for all the costs associated with the Farley Plant, while AEC, on the other hand, retains what is in effect an option to buy an ownership interest while it avoids sharing any of the risks or costs associated with continued reliable operation of the Farley Plant. 4/

4/ The current state of uncertainty may also serve AEC's economic interest. According to APCO's studies, if AEC were to purchase an ownership interest in the Farley Plant in 1984 at any price equal to or greater than APCO's cost attributable to the interest transferred, under any of several assumptions, AEC's average power cost would increase in the near term. A "cross-over" point would probably be reached at some time in the late 1980s or early 1990s, and thereafter ownership of the Farley Plant would probably reduce AEC's average power costs. This situation exists because any interest in the Farley Plant acquired by AEC would be used to replace wholesale power now purchased by members of AEC from APCO. APCO's wholesale rates are very low at the present time because a large percentage of the generation used by APCO consists of coal plants installed at the lower costs that prevailed in the 1950s, 1960s, and 1970s. As new capacity is acquired by APCO, its wholesale rates will increase. On the other hand, absent the need for major repairs or capital improvements, the fixed costs

The uncertainty is clearly unfair to APCO and can only be removed by the Commission's clarification of the precise meaning of the terms of the License Condition and a determination by the Commission of what APCO is required to do in order to comply with the License Condition.

II. Authority to Issue A Declaratory Order

The Commission clearly has the authority to issue a declaratory order in this situation. Under Section 181 of the Atomic Energy Act of 1954, as amended, the provisions of the Administrative Procedure Act apply to all "agency actions" taken by the Commission under the Atomic Energy Act. 42 U.S.C. § 2231. Under the terms of the Administrative Procedure Act the Commission "may issue a declaratory order to terminate a controversy or remove uncertainty." 5 U.S.C. § 554(e). The Commission itself has previously held that it "has undoubted authority" to issue such orders. Kansas Gas and Electric Company (Wolf Creek 1) CLI-77-1, 5 NRC 1, 4 (1977). As a policy matter, the Commission has also encouraged the use of declaratory relief in NRC proceedings in order to permit the "early resolution" of issues. Id. at 5.

Other federal regulatory agencies have utilized their declaratory powers to clarify prior rulings and orders and to interpret the terms and conditions of their own licenses and certificates. See e.g., Atlantic Freight Lines, Inc., 51 MCC 175

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attributable to the Farley Plant should remain relatively constant over the life of the Plant.

(ICC, 1949) (holding that an agency may properly issue an interpretation of its own order); Western Radio Corp., 14 Ad L 2d 479, 481 (FTC, 1963) (holding that a respondent may request the Commission's advice as to whether a contemplated course of action will constitute compliance with an outstanding cease-and-desist order); Archie's Motor Freight, Inc. (ICC, Div. 1, 1957) (holding that the ICC may on proper request interpret a certificate previously granted by it to a motor carrier). Reviewing courts have also approved of the regulatory agency practice of granting declaratory relief to licensees seeking clarification of prior orders or seeking to remove uncertainties concerning activities permissible under their licenses. See Southern Railway Co. v. United States, 412 F. Supp. 1122 (D.D.C. 1976), where the court approved the ICC's issuance of a declaratory order resolving a dispute among carriers as to interpretation of a prior ICC order approving shipping contracts. See also Chisholm v. F.C.C., 583 F.2d 349 (D.C. Cir. 1976) (FCC action in issuing a declaratory order modifying its previous interpretation of the "equal time" provisions of the Communications Act is valid where taken to eliminate uncertainty.)

As the recent correspondence between the parties (See Appendices 13 and 14) illustrates, and as Section III of this petition amply demonstrates, controversy and considerable uncertainty exist here, arising out of a corflict as to the proper interpretation to be given a License Condition imposed under a prior NRC order. In such circumstances, the issuance of

declaratory order by the Commission would be particularly helpful and appropriate. Issuance of a declaratory order affords, by far, the most efficient and expeditious method for resolving the controversy in this case and providing the parties with a mechanism for settling their differences over the proper interpretation of the License Condition.

The License Condition and the resulting negotiations between APCO and AEC followed one of the most complex and extensive proceedings ever conducted by the Commission. Attempting to resolve the differences between APCO and AEC regarding the proper interpretation of the License Condition by means of another formal adjudicatory proceeding, 5/ would benefit

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5/ AEC has filed a request, dated June 29, 1984, for enforcement action pursuant to 10 C.F.R. § 2.206. An enforcement proceeding is perhaps the most inefficient procedure imaginable for interpreting the License Condition. It is likely to involve lengthy consideration by the Commission Staff followed by an evidentiary proceeding before an Atomic Safety and Licensing Board, further proceedings before the NRC's Appeal Board, and, ultimately, review by the Commission.

APCO does not seek to avoid answering for its efforts to date to implement the License Condition; the Commission is always free to seek to punish a licensee for a deliberate violation of its license obligations. However, to delay a Commission decision interpreting the License Condition until the enforcement process has run its course would be inefficient and unfair. After the Commission has issued a declaratory order interpreting the License Condition, the Commission, or its delegate, can consider whether any punitive action against APCO is warranted, in light of the guidance provided by the declaratory order. APCO is confident that whoever decides that question will conclude that no such action is justified.

Accordingly, APCO urges that any question of action under 10 C.F.R. Part 2, Subpart B be held in abeyance until the Commission has issued the requested declaratory order.

no one. There is simply no need to resort to another time-consuming, personnel-consuming and resource-consuming trial type adjudicatory proceeding in order to resolve the matter at hand.

We recognize, however, that the Commission will require additional information concerning the various interpretations of the License Condition that have been proposed by the parties before it will be in a position to issue a declaratory order. APCO therefore proposes that the Commission issue a notice of receipt of this Petition which would provide an opportunity for submission of comments by all interested parties and direct that all such interested parties file memoranda, together with any supporting affidavits and exhibits, relating to the issues raised by this Petition, in accordance with the following schedule:

> APCO Memorandum -- 30 days after date of publication of the notice.
>
> Memoranda by interested parties, including AEC, other than the NRC Staff -- 60 days after date of publication of the notice.
>
> NRC Staff Memorandum -- 90 days after date of publication of the notice.
>
> APCO Reply Memorandum -- 120 days after date of publication of the notice.

The Commission could then appoint a special master, perhaps an Administrative Law Judge of the NRC, to review the memoranda submitted and conduct any further investigation of the issues deemed necessary by the Commission. The Commission could empower the special master with authority to require or permit the submission of such additional information or memoranda as

appropriate, to create a record on which the Commission can resolve the issues presented in this petition. Upon completion of the fact gathering process, the special master would submit a report to the Commission. This report could clarify the issues for Commission decision and contain proposed findings as to any factual matters that need be resolved in order for the Commission to reach and dispose of these issues. Thus, the Commission itself could decide the basic questions concerning the meaning of the License Conditions without expending any unnecessary time on subsidiary matters. 6/

The designated special master could take evidence and require additional submittals from the parties, but he would not be required to conduct a formal adjudicatory proceeding with the attendant rights of discovery, testimony, and cross-examination that generally prevail in NRC adjudicatory proceedings. A less than full-fledged procedure, characterized as "investigative" in nature, was previously approved by the Commission in Consolidated Edison Company (Indian Point 2), CLI-81-1, 13 NRC 1, 5, ft. 4 (1981). See also Consolidated Edison Company, CLI-81-23, 14 NRC 610 (1981), revising footnote 4.

6/ The interpretation ultimately given the License Condition involves basic policy questions of fairness to two groups of ultimate customers, APCO's and AEC's. We urge that these judgments be made by the Commission itself and not be delegated, even in the first instance to the special master. Thus, APCO's proposal is that the special master prepare a report that enables the Commission to reach the policy questions efficiently, not an initial decision in which he undertakes to recommend policy.

Since a declaratory proceeding to resolve conflicting interpretations of an NRC license condition would not involve "the granting, suspending, revoking, or amending of any license or construction permit . . .", 42 U.S.C. § 2239(a)(1), neither the Atomic Energy Act nor the Administrative Procedure Act require procedures more formal than those proposed. 7/ The Commission has the authority, therefore, to fashion fair and efficient informal procedures, which do not offend the requirements of due process. 8/

The adoption of the foregoing schedule by the Commission would comport with all applicable legal requirements, provide all interested parties with an opportunity to be heard, and, just as importantly, ensure that this issue is resolved in a timely and efficient manner.

7/ The trial type hearing procedures specified in the APA apply only to adjudications "required by statute to be determined on the record after opportunity for an agency hearing." 5 U.S.C. § 554(a). Where, as here, 42 U.S.C. § 2239(a) does not apply, an "on the record" hearing is not required, and the APA is silent as to adjudicatory procedures. Illinois v. NRC, 591 F.2d 12, 13-14 (7th Cir. 1979). The procedural requirements contained in the Commission's Rules of Practice, 10 C.F.R. Part 2, Subpart G, are also inapplicable. Id. See 10 C.F.R. § 2.700, defining the scope of the subpart.

8/ Even when a proceeding involves an amendment to a license and thus is subject to Section 189 of the Atomic Energy Act, 42 U.S.C. § 2239(a)(1), informal notice and written comment procedures have been held to satisfy the demands of due process as well as the mandates of the Atomic Energy Act and its implementing regulations. City of West Chicago v. NRC, 701 F.2d 632, 646-47 (7th Cir. 1983).

III. Matters in Dispute Between APCO and AEC

The following is a summary of the principal matters that APCO believes are in active dispute between APCO and AEC concerning the terms and conditions of the Purchase and Ownership Agreement. 9/ It is not APCO's purpose here to argue the merits of these issues; that would be done by all parties in the memoranda submitted to the Commission as described in Section II, above. The purpose of the following is to acquaint the Commission with the nature of the principal matters clearly in dispute and to demonstrate the need for declaratory relief.

1. Ownership Interest to be Transferred

APCO's offer to sell an ownership interest is based on a sale of 6.26% of the Farley Plant. AEC contends the figure should be 6.70%. The difference reflects a dispute over the interpretation of the License Condition, which bases the share to be sold on the relative sizes of the peak loads of AEC and APCO, not those of other parties. AEC derives its higher percentage by including firm power sales by the Southeastern Power Administration to certain of AEC's wholesale customers within the firm load served by AEC. APCO's method measures firm load commitments of AEC and APCO at the time of their respective peaks in 1976.

9/ As Appendices 8, 9, 13 and 14 reflect, other, less fundamental disagreements also exist between the parties.

2. Initial Sale Price

The price contained in APCO's initial offer was $1568.00 per kilowatt predicated on the nameplate rating of the plant, which is well below the reasonable value of the completed plant. The price gave weight to APCO's actual costs, as well as to the fact that APCO's investment was made in 1970-1981 dollars, while the sales price will be paid in considerably less valuable 1984 dollars. It also reflected that APCO suffered the considerable risks of financing and constructing the nuclear plant to completion.

AEC has responded to this initial offer, not with a counter offer, but with a statement of philosophy. Notwithstanding the language of the License Condition, AEC has refused to agree to payment of a price even approaching APCO's actual costs. Rather, it asserts that it will pay only that amount which it would have paid had it purchased, in 1971, a 6.7% interest in the plant at AEC's cost. While AEC has not revealed what this figure might be, it is beyond question that the amount will not even compensate APCO for its actual costs to date.

3. Security Arrangements

AEC's balance sheet reflects that it has a "negative equity" - that is, its liabilities exceed its assets. 10/ APCO has therefore requested that AEC provide some security for its share of the future ongoing operating costs of the plant, as well

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10/ APCO has in excess of $1 billion in equity standing behind its obligations, compared to the negative equity position of AEC.

as the decomissioning costs once the plant stops producing electricity. Several methods of providing security have been suggested. AEC has failed to provide any concrete response on this issue.

4. Participation in Day-to-Day Operation of the Farley Plant

AEC insists that it be permitted to station a representative at the Farley Plant site on a permanent basis. APCO believes that this would inevitably result in "interference in the day-to-day operations of the plant," in violation of the License Conditions. APCO has offered to provide AEC with other means of keeping closely informed of plant operations, including periodic reports and site visits which do not interfere with APCO's operation of the Farley Plant or jeopardize safety. In the interest of safety and efficiency of plant operations, APCO is convinced that only one owner/operator should be on site. AEC has made no attempt to justify its insistence on the most intrusive alternative.

IV. Terms of the Proposed Declaratory Order

APCO requests that the Commission declare the following:

(1) APCO's offer to sell a 6.26% undivided interest in the Farley Plant for a price of $168,865,000.00 and on the terms and conditions provided in the Purchase and Ownership Agreement,

the Operating Agreement, and the Nuclear Fuel Agreement appended hereto is a reasonable, good faith business offer which complies with APCO's obligation under the License Condition.

(2) If the Commission is unable to reach, without qualification, the conclusion stated in (1), above, APCO requests, in the alternative, that the Commission provide guidance as to the additional or different terms that APCO is required to offer in order to effect compliance with the License Condition.

(3) In either event, APCO requests that the Commission declare that APCO's obligations under the License Condition shall be fulfilled by offering to AEC, within sixty (60) days of the effective date of the Commission's final order on this Petition, a copy, executed by APCO, of each of a Purchase and Ownership Agreement, an Operating Agreement, and a Nuclear Fuel Agreement in the form appended hereto, modified to the extent necessary to comply with any ruling of the Commission in response to item (2), above, unless, within sixty (60) days of its receipt thereof, AEC accepts such offer by delivering to APCO such tendered agreements, fully executed by AEC.

V. Conclusion

For the foregoing reasons, APCO respectfully requests that the Commission adopt procedures similar to those suggested in Section II, above, and, following such proceedings as may be appropriate, issue a declaratory order addressing the issues raised in this Petition.

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July 3, 1984

AFFIDAVIT OF H. ALLEN FRANKLIN

My name is H. Allen Franklin. I am Executive Vice President of Southern Company Services, Inc. ("SCS") which is the service company organized pursuant to the authorization of the Securities and Exchange Commission under the Public Utility Holding Company Act of 1935 to perform services for the operating companies of The Southern Company. Prior to accepting my present position in May, 1983, I was Senior Vice President of Alabama Power Company ("Company" or"APCO") where I had responsibility, among other duties, for planning of the Company's bulk electric power supply system, including the generation and transmission facilities.

Most of my career in the electric utility industry has involved system planning, including the projection of expected demand and energy usage by customers and evaluation of alternative means to satisfy such requirements. This task involves determining the price for alternative resources and remaining abreast of the prices at which utilities in the region can generate and sell electricity. While at APCO, and in my present job with SCS, my responsibilities have included negotiations to acquire generating facilities; to sell ownership interests in generating facilities; to sell bulk power from the facilities of APCO (such as the unit power sales with Florida Power & Light, Jacksonville Electric Authority in Florida and Gulf States Utilities); and to purchase power from others (such as cogenerators).

In mid-1981, I was in charge of a special task force engaged in the development of a proposal for the sale of a joint ownership interest in generating facilities to the Alabama Municipal Electric Authority, a newly formed organization in Alabama whose members included several wholesale customers of APCO. In the development of this proposal, we conducted a survey of the manner in which joint ownership arrangements had been developed by other utilities. In August, 1981, shortly after the license was amended requiring APCO to offer to sell an ownership interest in the Farley Nuclear Plant to Alabama Electric Cooperative, Inc. ("AEC"), Mr. Farley, President of APCO, asked me to expand my assignment to include the development of a basis for an offer to sell an ownership interest in the Farley Nuclear Plant to AEC.

I. Background:

APCO initiated planning for the Farley Plant in 1968. A certificate of convenience and necessity to build Unit 1 of the Farley Plant was issued by the Alabama Public Service Commission ("APSC") in 1969. The Company entered into a contract with Westinghouse Electric Corporation in 1969 for the purchase of the nuclear steam supply system and the turbine generators.

The Company received its Operating License for Unit 1 in June, 1977, following the completion of the antitrust hearings by the Atomic Safety and Licensing Board. Those hearings resulted in the issuance of an Order requiring APCO to sell to

AEC unit power from the Farley Plant at APCO's cost, including the cost of money invested. The license condition was as follows:

> Licensee will sell to Alabama Electric Cooperative, Inc. ("AEC"), unit power from Units 1 and 2 of Joseph M Farley Nuclear Plant. The amount of capacity to be sold by Licensee from such units to AEC shall be an amount based on a ratio of (a) the aggregate coincident demand of all wholesale-for-resale members of AEC in Alabama during the hour of peak demand on the electric system of Licensee in 1976 to (b) the sum of such coincident demands of AEC and the territorial peak-hour demands of Licensee (excluding therefrom the peak-hour demands imposed by members of AEC upon the electric system of Licensee) during the hour of peak demand on Licensee's electric system in 1976. Contractual arrangements will be entered into between Licensee and AEC by the terms of which AEC will be entitled to purchase and receive the percentage of electrical output of the respective Farley units determined in accordance with the foregoing ratio. Such output from the respective units will be supplied by Licensee to AEC for the entire commercial service life of the particular units. Such contractual arrangements will also provide that AEC shall pay Licensee on a monthly basis for the capacity portion of such unit power, amounts representing the percentage of Licensee's fixed costs in such nuclear units based upon the ratio described above. Such contractual arrangements shall also provide that AEC shall pay Licensee on a monthly basis for the energy portion of such unit power, amounts representing the percentage of Licensee's variable costs incurred in the operation of such units based upon the ratio of energy generated for AEC's account to the total energy generated by such units during the billing month. The provisions of such contractual arrangements shall clearly provide that the net effect of such payments to be made by AEC shall be that AEC will pay its proportionate share of Licensee's total costs related to such

> nuclear units including, but not limited to, all costs of construction, installation, ownership, licensing and operation of such units, but no more than such proportionate share. The contracts covering such unit power shares shall embrace pricing and charges reflecting conventional accounting and rate-making concepts established and applied by the Federal Power Commission or its successor in function, and any disputes concerning the identification or application of such concepts shall be determined by and in accordance with procedures of the Federal Power Commission or its successor in function.

Pursuant to the license condition, APCO wrote AEC in October 1977, making a detailed proposal to AEC for the sale of unit power. In that proposal, Mr. R. E. Huffman offered to furnish AEC any information which AEC desired in connection with the plant. Under this proposal, AEC would have obtained power from the Farley Plant at the same costs which APCO obtained power. A unit power arrangement envisions that the owner of the plant invests debt and equity capital secured by the owner. AEC would have paid, under such proposal, the cost of capital which APCO invested in the plant, including the interest on debt and the return on equity. The APCO unit power proposal was in line with unit power sales contracts which have been approved by FERC and the methodology followed by FERC.

AEC responded to APCO's offer saying it was giving the proposal to its lawyers and consulting engineers to study. In January 1978, AEC again wrote saying its lawyers and engineers had been preoccupied but that they were going to meet soon and would contact the Company concerning the proposal. AEC never

sought clarification, discussions, or negotiations in any manner concerning the Company's 1977 unit power sale proposal for the nearly four years it was on the table prior to the June 30, 1981 Atomic Safety and Licensing Appeal Board ("ALAB") license revision. Nothing else was heard from AEC concerning access to power from the Farley Plant. To my knowledge, there has never been any suggestion by AEC that APCO was in violation of its license conditions during the period June 1977 through August 1981.

In 1981, the second unit was ready for fuel loading and an operating license, NPF-8, was issued on March 31, 1981. That license also contained the Order of the NRC that APCO offer to sell to AEC unit power from the plant. The October, 1977 unit power offer to AEC was still outstanding at that time. The offer covered both Unit 1 and Unit 2. During all of this time, APCO had financed the Farley Plant with capital obtained by it from debt and equity investors as was expressly contemplated by the NRC License.

On June 30, 1981, four years after the operating license for the first unit had been received, the ALAB issued an order requiring that the license condition be revised to require APCO to offer to sell AEC an undivided ownership interest in the plant. On August 10, 1981, the NRC issued Amendment No. 22 to Operating License NPF-2 and Amendment No. 4 to Operating License NPF-8. The revised language of the condition is as follows:

> Licensee shall offer to sell to AEC an undivided ownership interest in Units 1 and 2 of the Farley Nuclear Plant. The percentage of ownership interest to be so offered shall be an amount based on the relative sizes of the respective peak loads of AEC and the Licensee (excluding from the Licensee's peak load that amount imposed by members of AEC upon the electric system of the licensee) occurring in 1976. The price to be paid by AEC for its proportionate share of Units 1 and 2, determined in accordance with the foregoing formula, will be established by the parties through good faith negotiations. The price shall be sufficient to fairly reimburse Licensee for the proportionate share of its total costs related to the Units 1 and 2 including, but not limited to, all costs of construction, installation, ownership and licensing, as of a date, to be agreed to by the two parties, which fairly accommodates both their respective interests. The offer by Licensee to sell an undivided ownership interest in Units 1 and 2 may be conditioned, at Licensee's option, on the agreement by AEC to waive any right of partition of the Farley Plant and to avoid interference in the day-to-day operation of the plant.

In October 1981, shortly after the NRC denied the Company's request for stay of the license condition, AEC wrote asking for cost information. That information was supplied, as was other specific cost information requested by AEC, in January and February 1982. AEC had turned over the information gathering responsibility to Southern Engineering Company, Inc., its consulting engineering firm. Much of the information requested by Mr. Jeff Parish of that firm was not available in the form requested. Mr. Parish was invited to come to Birmingham to look at the books and records of the Company. He finally agreed to do this in June 1982. The

Company expended a great deal of time in gathering and making available to AEC the information requested.

In May 1982, the Company became concerned that AEC's delay in looking at the available cost information would later be cited by AEC as a delay on the Company's part in pursuing the negotiations. Mr. Jesse S. Vogtle, Executive Vice President of APCO, wrote AEC in May 1982, attempting to open up areas of discussions on compliance with the license condition. A copy of that letter is attached as Attachment 1. AEC responded in June 1982 stating, among other things, that it would get in touch with the Company when it was ready to begin discussions. AEC's response is attached as Attachment 2. It was not until March 1983, some nine months later, that AEC indicated it was ready to begin negotiations. A meeting for such negotiations was scheduled on May 24, 1983, but was predicated on the condition that APCO furnish AEC a written proposal four weeks prior to the meeting.

II. Preparation for Proposal:

By August 1981, APCO had already begun its investigation of arrangements which other utilities had entered into for joint plant ownership, and that investigation was later intensified to focus on joint ownership arrangements involving nuclear plants. The Company, in the period between June 1981 and October 1981, was seeking to have the NRC stay the requirement to offer to sell pending appeal of the license condition. Even before the NRC declined to stay this requirement

we had begun our effort to comply if ultimately it were determined necessary.

A. Review of Other Joint Ownership Arrangements:

Our investigation of joint ownership transactions involving other utilities became a major factor in formulating our initial negotiating strategy. Several issues surfaced from our investigation: (1) With respect to price, in both instances which we reviewed involving sale of completed plant, the price was above the selling utility's cost, as shown on its books, and included fees or other payments over the depreciated book costs of the plants. Where units were sold during the construction of the plant, most involved payment to the lead utility of amounts in excess of book costs. These included such items as construction management fees, tax adjustments, adjustments for actual capital cost incurred prior to date of sale, entitlement fees or some other form of price adjustments. (2) Operation and maintenance costs and capital expenditures were shared on a pro rata basis. Some of the transactions involved the payment of fees to the operator of the unit (i.e., fees for management services, fuel procurement, design services, operating services, etc.). (3) Incremental costs, such as developing new accounting systems required as a result of the joint ownership, were specifically identified as the responsibility of the purchasing entity in some instances. (4) The non-operating owner was to indemnify the operator for risks associated with the non-operator's share.

In all of these sales of plant after construction had begun, the sales price was predicated on the seller's cost of capital. In no instance did we find a sale predicated on what the purchaser's cost of capital might have been during that pre-sale period.

B. Farley Nuclear Plant Characteristics:

In preparing our proposal, we also took into consideration the fact that the Farley Nuclear Plant was an unusually valuable plant compared to other nuclear plants of its vintage. Significant risks of plant licensing, construction, ownership and operation had been eliminated by 1981 when the license condition requiring sale was imposed. Planning for the Farley Plant was initiated in the same time frame as the Midland Nuclear Plant of Consumers Power Company, the Shoreham Nuclear Plant of Long Island Lighting Company and the Zimmer Nuclear Plant of Cincinnati Gas & Electric Company. The present status of these contemporaneous units depicts the risks to which the Company was exposed during the last 14 years.

The Farley Plant is comprised of two Westinghouse Pressurized Water Reactor (PWR) Units. The Construction Permit for both units was issued on August 16, 1972 by the NRC, although site work had begun long before that date. The first unit was placed into commercial service on December 1, 1977 and the second unit on July 30, 1981.

Both units have gone through extensive design review, operational shakedown, and both have been modified as a

result of the knowledge gained from operating experience throughout the industry, especially from the Browns Ferry fire and the Three Mile Island events. The plant has consistently received favorable ratings in performance and safety from independent review and inspection sources. Since the units have been in service, they have performed very well when compared to other PWR units in the nation. Unit 1 has a cumulative capacity factor of 61.0% through August 1984 despite the impact of several major outages caused by equipment failures and regulatory requirements. Unit 2 has a cumulative capacity factor of 85.9% through August 1984 and, in 1983, it was among the top ten units in the world ranked according to capacity factor. In comparison, the average cumulative capacity factor for all United States nuclear plants through 1983 (which is the latest available information) was 58.2%. Among Westinghouse PWRs greater than 400 MWe in size, the Farley Plant Unit 2 and Unit 1 rank number 1 and number 18, respectively, out of a total of 32 units, based on cumulative capacity factors through July 1984.

The second unit at the Farley Plant has benefited significantly from the experience gained during construction, startup, and operation of Unit 1. This experience in the form of improved design, trained personnel, and knowledge level has been demonstrated in the higher performance of Unit 2. There were five major areas where Unit 1 experienced problems and corrective actions taken for Unit 1 were incorporated into Unit 2 to improve its performance. These are as follows: (1)

Modification to hanger and anchor bolts, (2) modifications to eliminate potential turbine rotor cracks, (3) modifications to main generator to alleviate a potential electrical fault, (4) improvement to design on baffle joints to alleviate potential physical damage to fuel assemblies, and (5) utilization of upgraded control rod guide tube split pins. The corrective action described in item (1) was required in several other nuclear plants. Items (2) through (5) resulted from generic problems that were experienced by other Westinghouse PWR units. The risks and costs associated with eliminating these problems were borne by APCO and its customers during the early years of operation. Both Units 1 and 2 are now better performing and less risky units because of APCO's successful operation and modification of Unit 1 during the first few years of operation.

The Farley Plant is managed by experienced managers who are constantly striving for excellence in every area of plant performance and safety. The performance and safety of the plant is monitored closely to identify any trends that need management attention. A support organization of design engineers who have many years of experience with the plant is used to respond promptly to any design related problem or question. This depth of expertise and experience has contributed to the good performance of the Farley Plant.

In summary, APCO has put together a team which has produced a premiere plant. There is no longer any risk to the investor as to whether the plant will get an operating

license; there is no longer any risk that construction will be delayed or cancelled due to financial considerations; there is no longer any risk as to the actual construction cost of the plant; and as a result of the Company's efforts with Unit 1, there is a significantly reduced risk that the plant will be plagued with major operating problems that could impair reliability and cost effectiveness. It is clearly equitable that APCO receive some consideration in the sales price for the risks it has borne and for its successful lessening of such risks.

III. APCO's Proposal and Negotiations:

In accordance with our agreement with AEC, we mailed to AEC, on April 29, 1983, the joint ownership proposal for sale of an interest in the Farley Plant. A copy of that proposal is attached as Attachment 3. That proposal was conditioned on the outcome of the court appeal as suggested by the NRC and Justice Department.

A. Rationale Behind APCO's Initial Joint Ownership Proposal.

1. Negotiating Strategy: The negotiations in which I have previously participated almost always involved the same process. Each party sets priorities as to issues to be covered in the negotiations. Each party also develops a negotiating strategy--with the ultimate objective of reaching agreement on a contract which is equitable and workable over its term. Obviously, each party attempts to structure an agreement which is most favorable to its interest but

understanding that the agreement must be acceptable to both parties if it is to be viable.

Initial negotiating positions are established as a starting point for discussions--from which there is give and take on both sides as the parties converge on a mutually acceptable point. My experience has been that, in most cases, neither party fully achieves all of its objectives but, in those cases where agreement is ultimately reached, both parties feel that, in the whole, the agreement is equitable. My previous experience in negotiating fuel supply agreements and bulk power contracts is based upon this negotiating style and attitude, and it is in this spirit that we approached these recent negotiations with AEC.

2. Primary Objectives: The Company's primary objectives for a final agreement were (and still are):

a. To meet fully the Farley Plant operating license condition requiring the Company to offer to sell a portion of the plant to AEC, and to engage in good faith negotiations with AEC concerning such proposal.

b. To avoid any nonproductive interference in the management and/or operation of the Farley Plant which could affect adversely the continued efficient, safe operation of the plant.

c. To obtain adequate security that AEC could and would honor all future obligations associated with joint ownership of the nuclear plant so as

to shield our customers and investors from risks of AEC failing to meet such future obligations.

d. To mitigate, to the extent possible consistent with the license requirements, any adverse effects on our customers either now or at any time in the future.

e. To compensate properly the Company's investors for sale of a valuable asset and for risks and economic losses taken during construction and the early period of operation of the Farley Plant.

f. To compensate the Company, on a reasonable basis, for managing the operations of AEC's ownership interest in the plant.

B. Problems which Arose: We undertook to achieve the objectives listed above in our proposals to AEC and in our attempts at negotiations with AEC. While in some areas the Company and AEC have been able to narrow or eliminate the differences between their positions in negotiations, there are still significant issues on which there has been no convergence of the parties' positions in the negotiations. These areas all involve issues as to which AEC has demonstrated almost complete unwillingness to negotiate. It has adopted fixed positions and has refused to move away from those positions, even though the Company has indicated its willingness to compromise. These areas of AEC's inflexibility are

primarily the areas as to which AEC has complained in its June 29, 1984 letter to Mr. Richard C. DeYoung. Briefly stated, AEC complains of APCO's position during negotiations as to the following matters:

1. Pricing proposals.

2. Calculation of ownership share to be conveyed to AEC.

3. Security to be provided by AEC to cover obligations for uninsured contingent liabilities.

4. Affirmative assistance to AEC in persuading regulators and others to permit AEC to purchase part of the Farley Plant.

5. Responsibility of owners for liability arising from the plant ownership or operations.

6. Responsibility of AEC for incremental costs of owning or operating the plant which arise solely because AEC becomes a part owner.

C. Company's Position and Negotiation Status on Problem Issues.

As I explained earlier, the investigation of joint ownership transactions involving other utilities played a major role in establishing the Company's position in the initial proposal. Obviously, the transactions that were surveyed were, for the major part, finalized transactions that reflected the give and take of negotiation. Since the license condition states that the price "... will be established by the parties through good faith negotiations," it would have been naive to base the Company's initial proposal totally on a bottom-line position with no room to "give". Therefore, the Company's initial proposal was developed by considering

favorable concepts and provisions found in other transactions plus the specific conditions surrounding these negotiations. Our proposal was also influenced by the fact that the risks of the venture had been borne by APCO during the construction and early years of operation of the plant, and that the Farley Plant had turned out to be an unusually successful nuclear power plant.

From the beginning of negotiations with AEC, however, the Company has expressed numerous times that the initial proposal was a starting point for discussions and the Company was willing to negotiate.

I will undertake to describe the Company's position on each of the problem areas identified above as to which AEC has complained and describe what has taken place during the negotiations with respect to these issues.

1. Sales Price:

a. Guidelines for Sales Price: The operating license condition states that:

> The price to be paid by AEC for its proportionate share of Units 1 and 2, determined in accordance with the foregoing formula, will be established by the parties through good faith negotiations. The price shall be sufficient to fairly reimburse Licensee for the proportionate share of its total costs related to the Units 1 and 2, including but not limited to, all costs of construction, installation, ownership and licensing, as of a date, to be agreed to by the two parties, which fairly accommodates both their respective interests.

My interpretation of this language is that the price is to be a negotiated value at least sufficient to

cover the costs listed above, but the price would not be limited to these costs. This interpretation was reinforced by the Eleventh Circuit's language "... AEC would, of course, pay the reasonable value for this interest." Therefore, in the course of developing an initial sales price offer to AEC, we considered numerous factors including the estimated market value of the plant, reproduction costs, actual construction costs, traditional pricing practices for sale of assets between utilities, and pricing approaches for other joint ownership sales under similar conditions. One's first reaction in pricing any asset is to charge what it is worth--measured either by what the asset would bring on the open market or the cost to replace the asset. Certainly, this is the price the Company would expect from the sale of a portion of this plant or any other asset sold on the open market as a result of arms-length negotiations.

b. Rationale of APCO's Proposed Sales Price: With this background, we proceeded to develop a proposed sales price which recovered (a) the Company's direct and indirect costs of building the plant, (b) out-of-pocket costs associated with making the sale, (c) some compensation for the risks borne in building the plant, (d) reasonable compensation for management services, use of a valuable scarce site and entitlement to major equipment contracts, and (e) at the same time, gave partial recognition to the value of the asset.

The proposed sales price ($1,568/kw) offered in the Company's April 29, 1983, proposal was

developed by taking a price halfway between (a) a price ($1,413/kw) constructed using an estimate of APCO's Cost Related to the Plant, and (b) a price ($1,724/kw) based on an Estimated Reasonable Value of the Plant. The development of the proposed sales price is shown in Attachment 4.

(1) APCO's Costs Related to the Plant: This aspect of APCO's initial price proposal is reflected on Attachment 4, Sheet 2, and is the sum of: net book investment (original cost less accumulated depreciation), an amount for cost of capital in excess of that booked during the construction period, an amount to keep the Company whole after paying income taxes associated with the sale, an entitlement fee, compensation for unrecovered costs incurred by the equity stockholders during construction, and construction work in progress. In developing this initial proposal, the Company's accounting personnel reviewed the Company's records of costs incurred during construction and consulted with Arthur Andersen & Co. to assure that the total costs of the Company were included in the price. They recognized that adjustments of the nature described in Mr. Walker's affidavit must be made to the net book investment reflected on the Company's books if the price was to reflect the Company's total accounting cost of construction, installation, ownership, and licensing. The adjustments calculated by the Company personnel are shown in Attachment 4, Sheet 2 in the items entitled "Capital Costs During Construction in Excess of Booked" and "Adjustment for

Income Tax Effect". Like certain of the other elements of APCO's proposal, these adjustments were based on assumptions which were open to scrutiny and negotiations. There was never any real focus on these numbers by AEC during negotiations, however, since under the pricing theory which AEC has continuously demanded that we follow, APCO's total costs of construction were irrelevant. Dr. Cicchetti's affidavit discusses compensation of the equity shareholders for the risks that they bore in bringing the project to successful fruition. The amounts included in the proposal to cover that risk were also announced to be subject to negotiations. Again, no such discussions were held since AEC refused to even discuss a price based on APCO's total cost.

The entitlement fee which was included in the April 29, 1983 proposal represented 6% of the proposed price or a total of $99/kw. This proposed fee was designed to compensate the Company for management and construction services, provision of construction equipment, procurement services for major equipment contracts and access to a licensed and developed site. Similar fees were found in other joint ownership arrangements that were reviewed.

It is clear that the return on common equity provided in the AFUDC recorded on APCO's books during the construction period did not adequately compensate APCO's equity investor. Shown below is a summary of new issues of common stock issued by The Southern Company, APCO's parent, during the period of construction of the Farley Plant. This

list shows (i) the weighted average sales prices per share to The Southern Company for such issue, and (ii) the average net book value per share of common stock related to such issue. This list shows that almost all of the common stock issued during this period resulted in proceeds below book value. The "book value" of a share of common stock is the net value of the assets shown on the company's balance sheet divided by the number of shares of common stock outstanding. It is a measure of the underlying asset value of a shareholder's investment.

SUMMARY OF SALES OF SOUTHERN COMPANY COMMON STOCK

DURING THE CONSTRUCTION PERIOD OF THE FARLEY PLANT

Year	Number of Shares Sold	Weighted Average Sales Price	Average Book Value	Sales Price Above (Below) Book Value
1981	22,259,793	$11.50	$16.35	$(4.85)
1980	19,952,293	11.62	16.80	(5.18)
1979	6,642,714	12.47	16.80	(4.33)
1978	5,330,135	15.26	17.05	(1.79)
1977	13,965,355	17.03	17.21	(0.18)
1976	12,560,638	14.99	16.81	(1.82)
1975	11,496,495	12.54	16.89	(4.35)
1974	17,500,000	9.50	16.58	(7.08)
1973	10,500,000	14.88	18.22	(3.34)
1972	8,300,000	21.25	18.07	3.18
1971	7,000,000	19.25	17.08	2.17
1970	3,800,000	22.00	16.33	5.67
1969	2,500,000	26.38	15.21	11.17

When new shares of common stock are issued at such a low price that the issuer does not realize proceeds, per share issued, equal at least to the pre-existing book value of a share of stock, the book value of the shares held by existing shareholders is reduced, i.e., if the new number of shares outstanding is divided into the new net asset value (including the proceeds of the net issue), the result

will be a lower number than before the new stock was issued. This is called "dilution", and it obviously has a deleterious effect on holders of shares outstanding at any time.

(2) Estimated Reasonable Value - Depreciated Replacement Cost: It is difficult to determine with accuracy the current value of the Farley Plant without putting the plant up for sale on the open market. A substitute approach is the methodology using depreciated replacement cost. Depreciated replacement cost is the traditional method of transferring assets from one utility to another. The typical process is for the seller to determine the costs to replace, with like kind, the asset to be transferred, then depreciate this replacement cost value based on the remaining life of the original asset. Several transactions between the Company and AEC have occurred in the past using this method. One such recent transaction between the Company and AEC involved the sale to AEC of the Wiregrass ECI-Bay Springs 115 kV tap:

Original Cost	Replacement Cost	Depreciated Replacement Cost	Negotiated Sale Price
$73,256	$288,500	$216,500	$200,000

Within the last year, legislation in Alabama designed to eliminate the duplication of electric facilities has established depreciated replacement cost as the statutory basis for transfer of electric utility facilities. This compensation formula was insisted upon by the members of AEC in the discussions leading to the adoption of the statute, since it applied primarily to the sale of facilities owned by the cooperatives.

In order to obtain an unbiased, expert estimate of the depreciated replacement cost of the Farley Plant, EBASCO Services, Inc. ("EBASCO") was retained to make an independent assessment. A copy of EBASCO's report is attached as Attachment 5. EBASCO's work yielded an estimated depreciated replacement cost of $1,724/kw--assuming a July, 1983, commercial operating date. In my opinion, this is a conservative (low) estimate.

c. Reasonableness of APCO's Proposed Sales Price: Our immediate reaction to the requirement to sell an interest in the Farley Plant was to make an offer based on the reasonable value of the plant. If APCO could sell an ownership interest in the plant to another utility at market value, why offer it to AEC for less? When APCO has to build plant or buy capacity to replace the Farley Plant capacity sold to AEC, it will have to build or buy that capacity at current market prices for such capacity.

The replacement cost of the capacity was APCO's initial suggestion in May 1982 of the way to develop a price to AEC as implied in Attachment 1. AEC responded in June 1982 (Attachment 2) that it felt the proper way to price the capacity was to calculate a price as though AEC had invested in the plant since the early 1970's.

While the Company still felt that the replacement cost or reasonable value of the Farley Plant was the proper basis for pricing, in an effort to move negotiations along, it retreated from that position and in its April 29,

1983 offer proposed an initial sales price that was significantly below the true value of the plant.

The EBASCO study reflects a conservative estimate of the true value of the Farley Plant. For example, EBASCO assumed that all regulatory requirements were known and fixed at the start of engineering design and that no costs were incurred due to changes in regulatory requirements. In reality regulatory requirements change routinely with significant cost impacts during engineering and construction.

Also, the conservatism of this estimate is confirmed by its comparison with cost estimates from a recent study prepared for the Department of Energy ("DOE"). Attachment 6 shows the ranking from that study of 31 nuclear units scheduled for completion between 1984 and 1990, using cost estimates submitted at year ending 1982. The EBASCO estimate, adjusted to eliminate interest during construction and depreciation so as to make it comparable with the numbers used in the DOE study, was $1683. This estimate would be ranked #7 on this list indicating that there are only 6 other units in the country that have cost estimates lower than the EBASCO estimate. Since that study was performed, one of the units reported as being less expensive (Marble Hill) has been cancelled. Approximately 80% (25 units) of all units on the DOE list are estimated to cost more than the EBASCO estimate, some ranging to nearly 250% greater than the EBASCO estimate. The DOE study notes that cost estimates are increasing at a pace that requires that comparisons be made with estimates at the

same point in time. Experience shows that these estimates on the DOE study will probably increase. Were the same study made today, the EBASCO estimate probably would rank even lower. For these reasons and for reasons stated in Dr. Cicchetti's affidavit, I believe $1,724/kw is below the true value of the plant; but nevertheless, we used this as a proxy for the value of the Farley Plant. APCO's initial offer in the negotiations was $156/kw below this estimate of the plant value.

Obviously, there are many courses the Company could have taken in developing an initial sales price proposal which would yield different numbers. The approach taken produced a price which is well below the value of the plant and well below the Company's replacement cost. The Company's intent was, and is, to put a fair price proposal on the table and to negotiate in good faith. Unfortunately, the negotiations regarding price have failed to follow the traditional negotiation patterns.

d. <u>APCO Cost Factors Not Included Directly in Price Proposal</u>: I have discussed the actual mathematical computation of the Company's initial price proposal and its reasonableness compared to the real value of the Farley Plant. Our major concern was not the mechanics of a methodology, but instead to develop a composite price proposal which was fair and equitable and a suitable starting point for negotiations.

Several cost considerations influenced the Company's thinking as to the appropriate level for a fair and equitable price proposal. Even though these components were

not used directly in computing the initial price proposal, they do bear mentioning because of their influence. Two of these considerations were: (1) "Undepreciated Cost", and (2) "Cost of Early Years of Operations".

(1) Undepreciated Cost: An accounting item which was not addressed by either the license condition or the court opinion is depreciation. From an accounting sense, the plant's value is being decreased each year by application of depreciation, when in fact the true value of the plant is increasing as replacement costs escalate. It does not seem appropriate to reduce the sales price for depreciation, when in fact the value is increasing without some recognition of true value of the plant in determining sales price. Although, as stated earlier, the Company did not use this approach directly in the development of its proposed sales price, the concept did influence our thinking in deciding upon a price level appropriate for an initial offer.

(2) Cost of Early Years of Operations:

The second cost component which influenced our development of a sales price, but was not included directly, was the consideration of the effects of the Farley Plant on our customers and stockholders during the early years of operation.

Looking first at our customers, one can see that the Farley Plant had the effect of contributing to higher rates due to the high initial capital investment that went into the rate base. In other words, in its early

years the cost of power from the Farley Plant standing alone is higher than the system average cost of power which includes some very inexpensive fossil and hydro generating capacity. Therefore, the system average cost of power increased when the Farley Plant went into the rate base. However, as the investment in the Farley Plant is depreciated and as future higher cost generating capacity is added and as fossil fuel costs escalate, the cost of power from the Farley Plant standing alone crosses over and becomes less than the system average cost of power. The crossover point for the Farley Plant is projected to be in the late 1980's or early 1990's. This scenario has been repeated time after time for utilities when they construct new generating capacity. Customers pay the higher costs of early years of operation with the expectation that these higher early year costs will be more than offset by lower costs over the remaining life of the plant.

If, however, a portion of the plant is sold to AEC prior to the time the higher early year costs have been offset by lower future costs, the Company's customers, who have paid these costs, will be denied the opportunity to experience these lower future costs associated with the portion sold. AEC, on the other hand, will reap the future benefits (i.e., when the cost of power from the Farley Plant will be less than the system average cost of power) without paying the higher early year costs.

Secondly, looking at the stockholders, one can see that the Farley Plant had a detrimental

effect in that the Company was unable to achieve timely and adequate rate relief to cover the cost of the Farley Plant units as they went into commercial operation.

The only way the stockholder may be able to recover these early year losses would be for the stock price to recover to a level that makes up the deficiency experienced in the early years. However, if the investment is sold off prior to this occurring, these losses are locked in and the stockholder forever suffers a loss for his willingness to finance the construction of the Farley Plant.

AEC should compensate the Company's customers and stockholders for carrying these early year costs. As mentioned before, these costs were not used directly in computing the sales price to AEC; however, this certainly is added justification for a price above pure accounting costs.

e. Negotiations on Price Between APCO and AEC:

(1) Positions Taken in Negotiations: I, and other representatives of the Company, expressly stated at numerous times in every one of the negotiating sessions we had with AEC that our price proposal was intended as a starting point and that selling price was negotiable. Representatives of AEC repeated in the first negotiating session in May 1983 what it had stated in its letter to APCO in June, 1982; that is, the price must be based on the principle that AEC should pay no more than as if its lower cost of capital had been used to finance its proportionate share of the cost of design,

licensing, equipment purchases, construction and other costs associated with the plant. This approach would obviously result in the Company not even recovering its direct out-of-pocket cost of building the plant and severely penalize both the Company's customers and stockholders. Since this price is clearly inconsistent with the license condition and unprecedented in any previous transfer of assets between utilities of which I have knowledge, I thought AEC's position was simply part of a negotiating strategy aimed at pulling the Company off its offer. Nevertheless, we felt it important that AEC at least give us the dollar figure which would be produced by its theory before responding with a counter offer. Such a dollar figure was never forthcoming.

During the second negotiating session at the Southern Engineering offices in Atlanta held on June 29, 1983, it became clear that AEC had no intention of negotiating price. During that session, representatives of AEC stated that they would only pay a price (which was not quantified) based on the hypothetical conditions which would have existed had AEC become a joint owner at the time construction began. They further stated that they had no interest in considering any price above that level and, if the Company would not accept AEC's pricing principle, it was useless to continue negotiations.

The Company suggested that if AEC was unwilling to negotiate price, then the parties would have to go to NRC for a ruling; therefore, the negotiators should

temporarily put the price issue aside and attempt to negotiate agreements in those areas where agreement appeared possible and narrow the unresolved issues before going to NRC. AEC agreed and discussion on other issues continued. To this date, AEC has not given the Company a counter offer to the price offered in the Company's April 29, 1983, proposal.

In June 1984, APCO made one more approach to AEC to explore agreement on price. APCO's thought was that agreement could more likely be reached on price if the discussions involved a smaller negotiation team from each side. We suggested, therefore, that two representatives from APCO meet with two from AEC in Montgomery. AEC finally agreed to that meeting. I was not in that meeting; however, it was reported to me that AEC again failed to give us a dollar amount which it would pay for the plant or agree to consider any proposal which did not assume, contrary to fact, that AEC commenced its pro rata investment in the plant starting in the early 1970's.

I have participated in numerous negotiations in several areas of the Company's business but these negotiations with AEC have been unique. I have never been involved in negotiations in which the key item to be negotiated--price--was proclaimed by one party to be non-negotiable from the very beginning of negotiations. This position is obviously unreasonable in view of the License Condition mandate that "... price ... will be established by the parties through good faith negotiations." In retrospect, AEC's non-negotiable

position on price clearly doomed the negotiations to failure before they started.

It became apparent in late June 1984 that the NRC would ultimately have to clarify the meaning of the License Condition as it relates to price. It was at that time that AEC announced it was planning to file a petition for enforcement action against the Company because of the Company's failure to accede to AEC's theory on pricing. APCO had recognized the possibility of reaching an impasse as to price at an earlier date and had determined that a declaratory order should be sought at the appropriate time. On July 3, 1984, a petition for such an order was filed seeking to obtain the NRC's interpretation of the License Condition.

(2) Need to Expedite Sales Transaction: In an effort to understand better the apparent conflicting positions taken by AEC--i.e., a stated desire to expedite the negotiations but taking an intransigent position on price which halted any progress--I asked APCO's System Planning Department to compare the cost of power from the Farley Plant to APCO's wholesale rates. AEC's stated intent is to purchase a portion of the Farley Plant to serve member loads now served by the Company under wholesale rates. This, of course, would be advantageous to AEC's member cooperatives only if AEC's cost of power from the Farley Plant is less than the Company's wholesale rates.

We considered three prices to evaluate the crossover point for this analysis. These three

prices were the proposal, twenty percent over the proposal and twenty percent under the proposal. The results of this analysis are shown in Attachment 7.

Even with the sales price assumed for the twenty percent under the proposal case, which would be obviously punitive to APCO, AEC's cost of power from ownership in the Farley Plant is more expensive than wholesale power from APCO for several years. This is due to the fact that wholesale rates are based upon embedded costs of all the Company's generating resources--which includes older, depreciated, very inexpensive coal fired units and very inexpensive hydro capacity. In the future, as new higher cost generating plants are built and as inflation impacts fossil fuel costs, the wholesale rates will become more expensive to AEC members than power costs from ownership in the Farley Plant. The optimum time from AEC's standpoint for AEC to purchase a share of the Farley Plant is when ownership becomes less expensive than Alabama Power's wholesale rate-- the alternative available to those of AEC's member cooperatives who now represent approximately 3% of APCO's total electric sales. Even though we had to make several assumptions in this analysis, including AEC's cost of capital, I believe that this analysis indicates that the optimum time for AEC to buy into the Farley Plant is still several years down the road. This economic reality apparently motivates AEC to avoid reaching an early agreement. AEC's fixed, non-negotiable position on sales price would seem

to reflect this motivation. If AEC succeeds in this posture, it will hold open its option to purchase a share of the Farley Plant at the optimum time for it.

The Company and its other customers are on the opposite side of this economic table. As is the case with most new generating plants (especially nuclear), the cost of power to all the Company's customers from the Farley Plant will be higher than the Company's average power costs for the early years of operation, crossing over and becoming less costly than average in the late 1980s or early 1990s. If a portion of the plant is to be sold eventually, it is then clearly in the Company's best interest to close the transaction at the earliest possible date; otherwise our customers must pay the cost burden of the Farley Plant during the time its power costs are higher than system average, and lose access to that portion of the plant's output which is to be sold to AEC when its costs are lower than system average. Therefore, contrary to AEC's motive, it is in the Company's best interest to complete the negotiations with AEC at the earliest date possible and not stall negotiations as charged by AEC.

2. Percentage Ownership: The license condition requires the Company to offer to sell ownership interest in the Farley Plant equal to "... an amount based on the relative sizes of the respective peak loads of AEC and the Licensee

(excluding from the Licensee's peak load that amount imposed by members of AEC upon the electric system of the Licensee) occurring in 197..."

Based upon load data supplied by AEC for its "on system" peak load, the Company initially computed AEC's percentage ownership entitlement to be 5.95%. During negotiations, AEC raised a question as to whether the AEC loads were at the delivery point or at the generator bus. Upon reviewing the source data, AEC's loads were found to be at the delivery point. For consistency of treatment with the Company's load data, losses were added to the AEC loads to determine equivalent loads at the generator bus. Using these revised data, the Company recomputed AEC's ownership share to be 6.26% and so advised AEC.

APCO's calculations are based on the respective peak loads of AEC and APCO. AEC would add an additional element, that is, the loads of Southeastern Power Administration (SEPA). AEC "off-system" member cooperatives connected to APCO's transmission system also purchase a part of their power at wholesale from SEPA. AEC contends that the wholesale loads served by SEPA should be included as part of the AEC peak load for the calculation of percentage ownership. However, the Company believes the firm load served by SEPA should be excluded from the calculation of percentage ownership ordered by the license condition because SEPA sells firm power through contracts which assure firm service to its wholesale customers. This SEPA preference customer load is the

responsibility of SEPA, not AEC or APCO, because SEPA has a contractual obligation to serve these customers. AEC does not serve this load and neither does the Company. AEC's position on this matter may now be moot. In its recent correspondence relating to the new contract between SEPA and APCO, AEC elected to consider loads served by SEPA capacity to be loads of SEPA, not loads of AEC. It would be inconsistent for AEC to continue to claim, for the purpose of the License Condition, that such SEPA loads were loads of AEC. A copy of the correspondence between APCO and AEC relating to this election is attached as Attachment 8.

3. Security for AEC's Contingent Liability: In contemplating the joint ownership arrangement between APCO and AEC, we tried to look objectively at APCO's exposure to additional costs resulting from such joint ownership and tried to find ways to minimize the risk that APCO would experience such costs. There are a number of events which may arise during operation of a nuclear plant which expose owners to tremendous costs which cannot be insured. The owners of Three Mile Island Unit 1 are faced with an uninsured cost of over $1 billion. The entire equity of the owners of that plant is on the line to assure payment of that cost.

Similarly, it is known that at the end of the life of the Farley Plant the owners will have to pay whatever the costs of decommissioning happen to be. The site cannot be abandoned by the owners simply because the money set aside for

decommissioning has been expended. The entire equity of the owner stands behind the decommissioning obligation.

In the above two examples, we also recognized two other important facts: (1) The owner cannot expect any future production from the plant so the temptation to try to avoid the expenditure may be great; and (2) if AEC successfully avoids paying its share of such costs, APCO will not be able to avoid such costs by telling NRC it is only responsible for 93.74% of the problem.

Recognizing this exposure to these added costs, we asked whether it was likely that AEC would seek to avoid its pro rata share of the responsibility. In analyzing the financial statements of AEC, it became clear that AEC and its members had little to lose in trying to avoid such exposure through bankruptcy or insolvency proceedings. Equity investors in APCO's system would place at risk over $1.5 billion if APCO were to try to avoid its obligations through bankruptcy. The recent financial statements of AEC reflect that it has a "negative equity". Because of this, there is no loss to the owners if the system goes into bankruptcy. The only motivation which would keep AEC from declaring bankruptcy in such instance would be a moral commitment not to try to avoid legitimate obligations.

Our concern on this point was heightened by the episode involving the financing of the Washington Public Power Supply units. There, certain participating utilities, including cooperatives were able to renege on their financial

commitments to these projects. These concerns drove us to request AEC to provide security for payment of these uninsured contingent liabilities which would place APCO in a credit position other than just a general creditor of AEC.

Several security arrangements were suggested by APCO, including obtaining a guarantee of AEC's obligation from the Rural Electrification Administration; obtaining a second mortgage (behind that of REA's) on the Farley Plant and the rest of AEC's system to assure payment of AEC's share of the cost; and obtaining a guarantee of payment from AEC's members. AEC initially stated that it would work to develop a method of providing some form of security; however, it later retrenched and stated that AEC had always paid its debt, therefore the Company should simply trust AEC to do the right thing.

In an effort to assure that our request to AEC was not an unreasonable request in the opinion of a banker accustomed to such risks, we requested that Mr. Philip C. Kron of Citibank, N.A. examine this issue. His affidavit confirms the reasonableness of the Company's concerns.

Again, the adamant refusal of AEC even to consider the legitimate request by APCO for security has complicated the negotiations and presents an unresolved issue.

4. Affirmative Assistance to AEC in Seeking Regulatory Approval: AEC has complained that APCO has "refused to agree in any way to assist in the gaining of necessary regulatory approval for AEC's acquisition of its ownership share." This is not true. Our position has always

been that we would furnish AEC any information concerning the Farley Plant which AEC needs in connection with any regulatory proceeding which AEC must pursue in order to acquire an ownership share of the Farley Plant. AEC raised this issue during negotiations demanding not only that APCO furnish any needed information and formal applications necessary for such regulatory proceedings, but also that the Company agree to advocate, in any such proceeding, the public need, wisdom and public interest associated with AEC becoming an owner of the Farley Plant. AEC's insistence that APCO agree to support affirmatively AEC's applications for regulatory approvals is, in my opinion, an unreasonable and unnecessary demand on AEC's part and was designed by AEC as an issue to prolong negotiations. The position of the Company on this issue was stated clearly on page 14 of the September 26, 1983 letter to AEC, a copy of which is attached as Attachment 9.

5. Liability of Plant Owners: AEC has also complained in its letter of June 29, 1984 of the Company's negotiating position concerning the allocation between the joint owners of liabilities arising from ownership of the plant. APCO's position on liability arising out of joint ownership is reflected in the comprehensive drafts of the Purchase and Ownership Agreement, the Operating Agreement and the Nuclear Fuel Agreement which have been sent to AEC and which are attached as Attachments 10, 11 and 12. AEC is plainly incorrect in asserting that APCO refused "to accept any responsibility to AEC for any gross negligence or reckless misconduct

by APCO in the operation of the Plant". Section 8.04 of the draft Purchase and Ownership Agreement sent to AEC in April of 1984 fairly and accurately allocates the risk of liability to third persons between APCO and AEC.

According to Section 8.04, APCO and AEC would share liability to third persons (other than liability for Willful Misconduct) in proportion to their respective ownership interests in the plant. This method of allocating the risks inherent in operation of the plant makes each joint owner responsible for its share of the costs of operation. The definition of "Willful Misconduct" contained in Section 8.04(b) has the effect of causing the parties to share, in proportion to their ownership interests, the risk that either of them would be vicariously liable for the gross negligence or reckless misconduct of one of their agents or employees. The Agreement only imposes complete responsibility for an act or omission on one party or the other when an officer for such party with policy-making responsibilities authorizes the act or omission.

In our view, the arrangement contemplated by Section 8.04 does no more than require AEC to bear the risks it would have to bear if it were both owner and operator. If AEC operated the plant, it too would run the risk that it would be held vicariously liable for acts of its agents or employees, which its management never authorized or even knew about. If APCO were required to bear the risk of vicarious liability associated with AEC's ownership share, the

agreements would give AEC a windfall with respect to third party liability solely by virtue of the fact that AEC was not involved in the operation of the plant. What will be avoided in Section 8.04 is an unfair situation in which APCO would have responsibility for 100% of the damages of any kind associated with the plant even though it has access to only 93.74% of the plant output.

APCO's drafts of the agreements impose complete responsibility on APCO for willful conduct that APCO's management is in a position to control. With respect to liability that is an inherent risk of doing business (i.e., the risk that one's employees will act recklessly or negligently) the Agreement provides for a sharing of such risk in proportion to the benefits to be derived from plant ownership.

The concepts embodied in Article VIII of the three draft agreements are not different from those which have been included in the arrangements between other joint owners of nuclear plants. It has been generally recognized as being unfair for the majority owner/operator to have responsibility to the other owners for all consequences of operations regardless of the actual control which the majority owner has over the events leading up to the incident giving rise to the damage. In most of the other agreements relating to joint ownership and operation of nuclear plants, the majority owner is protected against responsibility to the minority owner either through indemnification provisions or provisions embodying limitations on remedies or liability.

From a practical viewpoint, after the sale to AEC is made, APCO will still own approximately 94% of the Farley Plant. AEC's minority ownership would in no way reduce APCO's desire and incentive to operate the plant in the most efficient, safe and economical manner possible. In addition, APCO's draft Operating Agreement clearly states that APCO will not make any adverse distinctions in its operation of the Farley Plant because of AEC's joint ownership. See Attachment 11, page 3, Section 1.01(c).

Even without this protective covenant, APCO would have absolutely no reason to operate the plant in such a way as to harm AEC; but would, instead, have every reason to operate the plant just as it has to date. This operation would be to the mutual benefit of both joint owners.

We thought agreement had been reached on this issue and are surprised that AEC would criticize the negotiated position which protects AEC without exposing APCO to risks which are rightfully AEC's as a joint owner in the plant.

6. Responsibility for Ongoing Operation and Maintenance Costs, Capital Additions and Incremental Costs: The April 29, 1983, proposal is based on the principle that the continuing costs of owning, operating and modifying the Farley Plant should be shared by AEC and APCO based on their respective ownership shares. In this way, AEC and APCO would pay for their respective share of total costs only. All costs

for which APCO heretofore had sole responsibility would now be shared on a pro rata basis with AEC.

However, the proposal provided that APCO should not share in or in any way be responsible for costs that arise solely as a result of AEC becoming a joint owner. For example, solely in order to accommodate AEC as a joint owner, a new accounting system must be developed. Costs of this type are referred to in the proposal as "incremental costs" because they are costs that APCO would not have (and would not have to pass on to its customers) if APCO had total ownership. This approach maintains each joint owner in the position of being responsible for the total costs on an equitable basis because the "incremental costs" add no value that APCO or its customers could share in.

The continuing costs of operating the plant that would be shared ratably can generally be grouped into three categories: operation and maintenance, capital improvements, and nuclear fuel. APCO has been incurring the total costs for these areas because APCO has had total ownership and has been receiving any and all benefits derived therefrom. However, now APCO will continue to use its expertise and resources to perform all these functions but will no longer receive any of the benefits associated with AEC's pro rata share. Successfully operating a nuclear plant is one of the great challenges in our industry today, requiring a tremendous level of skill, dedication and expertise of employees at the plant level and extending to the chief executive officer of

the Company. APCO has therefore proposed that AEC pay appropriate fees to APCO for the services that will be provided to AEC in each of these three areas. APCO is not in the business of providing services to others at out-of-pocket cost. If APCO were to contract to provide services to an unaffiliated firm, the contracted price would certainly be at cost plus a fee. Such a fee is a reasonable requirement for APCO's dedication of its management and manpower expertise for the benefit of another company. The level of the fees in this initial proposal were clearly stated to AEC as being negotiable. APCO offered these as an initial point from which to begin negotiations. However, AEC has summarily rejected any consideration whatsoever of paying APCO a fee of any kind for APCO's services.

In lieu of specifying fees for services rendered as originally suggested in the Company's April 29, 1983 proposal, the drafts of the Operating Agreement (Attachment 11) and the Nuclear Fuel Agreement (Attachment 12) provided that AEC will pay, in addition to its pro rata share of all operating costs, an amount designed to cover costs which are not susceptible to precise quantification. The amounts proposed are 10% of AEC's operation and maintenance costs, 10% of AEC's new investment costs (capital improvements), and 1% of AEC's nuclear fuel costs. These amounts constitute a recognition that APCO's accounting system does not capture completely the total costs associated with the operation of the Farley Plant, particularly the cost of management attention

required for this plant compared to other plants. The amounts proposed will serve to reduce the likelihood that APCO unfairly bears a portion of AEC's responsibility for its share of total costs. The amounts proposed are fair and reasonable. For example, the 10% of operation and maintenance costs proposed by APCO equates to a smaller cost per kWh than the amount which FERC routinely allows for unquantifiable costs associated with transmission coordination transactions. It is clear that there are many more such unquantifiable costs associated with the nuclear production function than the transmission function.

The amounts proposed by the Company in the draft agreements are substantially less than the fees in the Company's initial proposal. Here, as in the case of sales price, the Company finds itself negotiating with itself since AEC's position on any type fee or recognition of unquantifiable cost was non-negotiable.

Conclusion

APCO entered into negotiations with AEC for a sale of a percentage ownership in the Farley Plant in a good faith effort to comply fully with the License Condition. The Company has endeavored to negotiate an agreement which satisfies the requirements of the License Condition and which, to the extent possible, minimizes any adverse consequences to our customers and investors. Any other approach would be an inexcusable abdication of management's responsibility to the

Company's customers and to those who have invested their money in the Company.

The Company has taken flexible positions on key issues and indicated a willingness to bargain in good faith with AEC to reach a mutually acceptable middle ground. AEC, on the other hand, has stated from the beginning that key issues, especially price, are not negotiable and that the Company must accept AEC's principles or AEC will seek to have those principles invoked by other means.

I feel that the Company's approach is within both the letter and intent of the License Condition which requires the parties to negotiate, while AEC's take-it-or-leave-it attitude clearly is not.

The Company has been and continues to be willing to negotiate a sale of a percentage ownership of the Farley Plant with AEC. Based upon experience to date, however, it is evident that clarification of the intent of the License Condition by NRC is required before any meaningful progress is possible.

ATTACHMENT 1

UNITED STATES OF AMERICA

BEFORE THE

NUCLEAR REGULATORY COMMISSION

STATE OF ALABAMA)

JEFFERSON COUNTY)

H. ALLEN FRANKLIN, being first duly sworn, deposes and says that he has read the Affidavit of H. Allen Franklin and that the matters and things set forth therein are true and correct to the best of his knowledge, information and belief.

H. Allen Franklin

Subscribed and sworn to before me
this the 8th day of October, 1984.

Jo Ellen P. Nelson
Notary Public

My Commission Expires: 5-30-87

Alabama Power Company
600 North 18th Street
Post Office Box 2641
Birmingham, Alabama 35291
Telephone 205 250-1000

ESSE S. VOGTLE
Executive Vice President

Alabama Power
the southern electric system

May 6, 1982

Mr. Charles R. Lowman
General Manager
Alabama Electric Cooperative, Inc.
P. O. Box 550
Andalusia, Alabama 36420

Dear Mr. Lowman:

We have been in communications with Mr. Jeff Parish of Southern Engineering concerning cost data relating to the Joseph M. Farley Nuclear Plant. We understand that he and his organization are representing AEC in preparing for discussion concerning implementation of License Condition 2F(2) which has been imposed upon the Farley Plant Operating License and, in addition to sending certain information to him, we have invited him to review the cost records about which he has inquired. In this connection, we are writing you to obtain your ideas concerning the license conditions as they involve relations between Alabama Power and AEC including the following questions:

1. Condition 2F(2) requires negotiations to establish the price to be paid for an ownership share in the Farley Plant. As you are aware, the sale of plant as required by this license condition will result in the need to replace the capacity sold with capacity costing in the thousands of dollars per kilowatt. This additional cost must then be recovered in our rates to our customers. We would be interested in getting your views as to how the price of the capacity to be sold to AEC should be established in view of the additional cost burden which the sale will impose on our customers.

2. We would also be interested in your views as to provisions to be included in any agreement for sale dealing with how such sale could be reversed at a later date should Alabama Power's appeal of the decision requiring imposition of the condition be successful. In this connection, we would appreciate your addressing the following questions: (a) From which entity would AEC borrow funds to secure the purchase price for the plant? (b) Would such lender require a mortgage on the property in connection with the loan; and if so, could advance agreement be reached with respect to release of such property from the mortgage upon

reconveyance of the property to Alabama Power? (c) Would such lender agree to an early repayment of the loan upon any subsequent reversal of the decision on appeal?

3. We need records and data reflecting the loads of AEC's wholesale customers in Alabama at the time of AEC's peak in 1976. As you are aware, the Appeal Board order penalizes the retail and other wholesale consumers of Alabama Power by accepting AEC's argument and requiring a sale which would allocate part of the Farley Plant to AEC's customers which the plant was not designed to serve. This was done not only by including in the calculation loads of AEC which were never intended to be served by the Farley Plant, i.e., the "on system" customers, but also, by allocating the plant on the basis of the non-coincident peak load of AEC rather than the coincident peak demand of Alabama Power's customers. While AEC has always rejected any notion that wholesale power cost should be allocated on non coincident peak demand, it ignores inconsistency with this principle when it seeks to penalize other customers in Alabama. We do need, however, to know what that non-coincident peak demand was in order to determine how much of a penalty the customers for whom the plant was designed to serve will have to suffer.

4. We would also be interested in your ideas concerning the timing of a sale. We would assume that if the response to this question were predicated on a rational economic evaluation, AEC would not be interested in any immediate sale since it would result in increased power costs over and above the power costs which AEC would otherwise experience. Nevertheless, we need to know your ideas in this respect.

If you would reflect on these matters and advise me of your thinking at your convenience, I would appreciate it. I would also appreciate your suggestions of a time, after Mr. Parish has satisfied himself with respect to cost data and after you have had a chance to respond to the above questions, that preliminary discussions could be held.

Yours very truly,

JSV/st

ATTACHMENT 2

Alabama Electric Cooperative, I
POST OFFICE BOX 550
Andalusia, Alabama 36420

June 4, 1982

Mr. Jesse S. Vogtle
Executive Vice President
Alabama Power Company
P. O. Box 2641
Birmingham, Alabama 35291

Dear Mr. Vogtle:

This is in response to your letter of May 6, 1982. Jeff Parish has contacted the Company regarding his visit to its offices to gather the information needed by AEC, and not yet furnished by the Company, for meaningful discussions regarding AEC's purchase of an undivided share of Farley Nuclear units 1 and 2. In response to your specific questions, we offer the following comments:

1. The claim in your letter that a sale of a share of the Farley units to AEC (which would enable the Company to be on belated compliance with its licenses to operate these units) would place a cost burden on the Company's customers is ludicrous. The Company has and will have excess capacity in substantially greater amounts than will be sold to AEC from the nuclear units.

AEC's capacity entitlement represents less than 1.5% of the Company's capacity at a time when the Company enjoys a 23.2% reserve margin and the Southern System pool has a 30% reserve margin. The Southern Companies subregion of SERC projects reserves from 39% to 30% for the 1982-1991 period. Most impressive are the hugh export sales being made by the Company and its affiliates--from 350 mw to 2000 mw to Florida Power and Light for 1983-1995; from 300 mw to 500 mw to the Jacksonville Electric Authority for 1983-1993; and 500 mw to Gulf States Utilities for 1984-1992. It is evident that the Company and the System are and will be capacity fat in the next decade.

Further, the Company has been on explicit notice from the Commission since the receipt of its construction permit for Farley unit 1 that it must conduct its planning and other activities taking into consideration the possible future imposition of conditions granting access to the Farley units to other systems. Thus, if the Company

management has deliberately ignored the Commission's warning, with the result that the sale of AEC's share of the nuclear units would produce any negative economic impact on the Company, that is a product of APCo's own management decision for which the Southern Company, as stockholder, must pay the price.

In no event will AEC compensate, or make whole, the Company for its management's decision to ignore the notice given it by the Commission. No replacement capacity needs of the Company may be taken into consideration in the cost to AEC of AEC's portion of the units. To do so would be contrary to the license conditions imposed on the Company because of its anticompetitive conduct. The purchase price of AEC's share in the units must be set at a level that avoids any economic penalty to AEC for the Company's anticompetitive refusal to grant access to the units from the early 1970's to the time of consummation of the sale.

However, if the Company persists in its claim that it has replacement capacity problems, AEC would be willing to discuss with the Company the early termination of Company service to certain distribution cooperative delivery points as a means of freeing up embedded-cost capacity to alleviate the Company's purported problem.

2. While it is extremely unlikely that the NRC's decision will be reversed on appeal, the Company's concerns can easily be resolved on this matter. It is our understanding that numerous joint ownership agreements provide for reconveyances under certain circumstances and so could the Farley ownership agreement. For example, the Wansley and Hatch Ownership Agreements between Georgia Power Company and Oglethorpe Power Corporation provide for reconveyance as do the Detroit Edison, Northern Michigan Electric Cooperative, and Wolverine Electric Cooperative Agreements regarding units Enrico Fermi Nuclear units No. 2. Similar clauses are contained in the Crystal River unit 3 and Catawba joint ownership agreements regarding units constructed by Florida Power Corporation and Duke Power Company, respectively. With respect to the contingency of extinguishing the right of a third-party security holder advancing funds to AEC, such security holder would be obligated to release such lien when the loan funds are repaid. For example, it is normal practice for the REA to have such clauses in its mortgages including those used to assist in the financing by cooperatives of nuclear joint ownership participation arrangements with investor-owned utilities.

AEC plans to borrow funds from the FFB through REA. A mortgage would be required and an advance agreement would be reached with respect to the release of property from the mortgage if a reconveyance to the Company were to become necessary.

3. Regarding paragraph 3 of your letter which addresses AEC's percentage ownership, your quibbles with the formula for ownership in the license conditions were best addressed to the NRC's Appeal Board when the matter was pending before it. We see no reason to debate the existing license conditions, and we hope that the Company intends to comply with them. Again, as we have said above, any economic "penalty" claimed by the Company is the direct result of its management's decision to take steps contravening the antitrust laws and should not be borne by AEC or the Company's customers.

We have calculated that AEC's peak load for use in computing percentage of ownership interest would be 410.9 megawatts. This was arrived at by taking the 60-minute system peak demand of 243.9 megawatts established on July 21, 1976, adding a calculated coincidental peak demand of 207 megawatts for the "off-system" member load, and subtracting 40 megawatts calculated as the Florida and industrial load contribution to the integrated system demand. Calculations and other data on this matter can be covered in detail when preliminary discussions begin.

4. Our review of the Farley nuclear units costs, which is not completed, indicates at this point that AEC would achieve favorable economies from the present acquisition of its share of the units.

After Mr. Parish completes his review of data in Birmingham, we shall contact you to establish a time and place for discussion of the acquisition.

Sincerely yours,

Charles R Lowman

Charles R. Lowman
General Manager

CRL:elf

ATTACHMENT 3

Alabama Power Company
600 North 18th Street
Post Office Box 2641
Birmingham, Alabama 35291
Telephone 205 250-1000

H. Allen Franklin
Senior Vice President

Alabama Power
the southern electric system

April 29, 1983

C O N F I D E N T I A L

Mr. Charles R. Lowman
General Manager
Alabama Electric Cooperative, Inc.
P. O. Box 550
Andalusia, Alabama 36420

Dear Mr. Lowman:

Section 2.F.(2) in each of the Operating Licenses issued by the Nuclear Regulatory Commission for Units 1 and 2 of Alabama Power Company's nuclear plant requires Alabama Power Company ("APCO") to offer to sell Alabama Electric Cooperative, Inc. ("AEC") a joint ownership interest in those units. In discussions with your counsel, it was agreed that we meet with you on May 24, 1983 to discuss such an offer. We are furnishing you in this letter the outline of an offer which APCO is making solely as a response to these license conditions.

As you are aware, APCO continues to disagree with the necessity for any license conditions to be imposed, and with the propriety of the conditions imposed, particularly the one requiring forced sale of the plant to AEC. Because of our disagreement, the appeal of the decision of the Eleventh Circuit Court of Appeals will be pursued. This letter and the discussions which follow between APCO and AEC shall not constitute a waiver of APCO's position with respect to the ongoing litigation. The outline of terms and conditions set forth herein forms the basis on which APCO proposes to sell an ownership interest in both units of the nuclear plant to AEC. Actual sale of such ownership interest shall be subject to a condition precedent that APCO's appeal of the Atomic Safety and Licensing Board's order is unsuccessful and the United States Supreme Court fails to require alteration of the requirements of Section 2.F.(2) of the licenses.

As you are aware, APCO has expressed concern for the past ten years that the sale of a joint ownership interest in the plant to AEC could result in increased costs to APCO and decreased nuclear plant safety because of shared managerial

responsibilities. We have been told repeatedly that neither concern is well founded. To assure that this involuntary sale of the ownership interest in the plant to AEC will actually avoid these problems (i.e., provides assurance that AEC's interest will not increase risks and avoids assumption by APCO of any risk of costs associated with the ownership share of the plant conveyed to AEC), the contractual arrangements will have to be carefully structured. With this objective in mind and subject to the reservations set forth above, as well as any other matters which may arise during negotiations that are necessary to achieve this objective, APCO is setting forth below an outline of the basis on which APCO will sell an ownership interest in its nuclear plant to AEC. This outline is subject to revision during negotiations to reflect matters not heretofore recognized as problems associated with the proposed joint ownership arrangement.

A. Sale of Ownership Interest in Plant Facilities:

APCO will convey to AEC an undivided ownership interest in Units 1 and 2 of the nuclear plant; the property constituting the plant to be conveyed being described generally below. The amount of the ownership interest to be conveyed shall be 5.95% which has been determined in accordance with the following formula:

$$\% \text{ Interest} = \frac{A}{A + B}$$

Where A = The sum of the 1976 peak hour loads of the wholesale for resale customers of AEC in Alabama served directly by AEC and the peak hour loads of the wholesale for resale members of AEC served by APCO.

B = APCO's 1976 territorial peak hour load (exclusive of loads of members of AEC served by APCO).

The sale of the property shall be based on payment at closing of the amount reflected on Exhibit 1 attached hereto. The price developed on Exhibit 1 considers both the reasonable value of the nuclear plant and all costs to APCO related to the plant. As you are aware, the Eleventh Circuit, in affirming the order of the Atomic Safety and Licensing Appeal Board requiring an offer for sale of an interest in the plant, stated that "AEC would, of course, pay the reasonable value for this

interest." We have secured from EBASCO Services, Incorporated, an engineering services organization which has expertise in nuclear plant costing methodologies, an estimate of the reasonable value of the plant. This estimate reflects a conservative judgment of the reproduction cost of the plant less depreciation. As you are aware, this methodology is commonly used for the valuation of utility property and is less than the amount which some jurisdictions have held just compensation in cases of forced sales of utility property.

APCO has also developed the total cost of the plant to APCO. Both the cost to APCO and the estimated reasonable value are shown on Exhibit 1. To arrive at the price at which the plant is being offered to AEC, we have averaged the EBASCO determination of reasonable value and the cost of the nuclear plant to APCO.

In addition, Exhibit 1 shows the breakdown of the price for the nuclear fuel component. All of these prices on Exhibit 1 are predicated on a June 30, 1983 basis and will, of course, have to be adjusted to the actual date of closing.

The contract for sale and deed shall be predicated on the following general principles:

1. Fee title only to land constituting the Security Protected Area of the nuclear plant site will be included in the sale. At APCO's option, AEC shall reconvey this interest in land to APCO for nominal consideration upon complete decommissioning. Facilities to be conveyed will be those improvements on the entire site, which shall include all facilities necessary for operations of Units 1 and 2. Included in the sales price shall be an amount necessary to acquire a contract right to AEC's pro rata portion of nuclear fuel (and nuclear fuel ingredients not yet incorporated in nuclear fuel).

2. All facilities shall be sold by quit claim deed on an "as is, where is" basis, with an express assumption by AEC of all risks associated with ownership, operation, and future maintenance of the facilities. In addition, there shall be an explicit negation of all expressed or implied warranties as to the condition and quality of the facilities.

3. AEC shall agree to accept the terms and conditions of, and agree to be bound by, all contracts which have been entered into or will be entered into by APCO or others on APCO's behalf in connection with the construction, operation and maintenance of the facilities or purchase of nuclear fuel or contract relating to any step in the nuclear fuel cycle. In the event APCO incurs any incremental costs under such contracts because of the sale of the interest in the nuclear plant to AEC, AEC shall bear the total responsibility for such incremental costs.

4. AEC shall be responsible for the total costs of any requirements for changes or alterations of the plant, APCO's accounting system or any other aspect of APCO's operations which result from AEC's acquisition of an ownership interest, such as, the cost of complying with requirements of REA as lender to AEC.

5. APCO, its agents, contractors and their employees shall be held harmless by AEC against any claim by AEC, its members or purchasers, their customers, and any other party for any cost or liability of any character as a result of the condition of the nuclear plant, including any patent or latent defects or any other condition of the facilities (including nuclear fuel) transferred, whether or not APCO, its agents, contractors and their employees are aware of such condition at the time of sale and whether or not such condition has been revealed to AEC prior to the sale of the plant. After sale of the interest in the plant to AEC, AEC shall be responsible for its pro rata portion of any liability to third persons which results from the plant whether or not such liability is traceable to causes which occurred before the sale of the interest in the plant to AEC.

6. APCO, its agents, contractors and their employees shall not be liable to AEC in any way as a result of the damages, costs or liability which AEC may incur as a result of any violation or infringement of a patent, trademark, service mark or proprietary agreements associated with the facilities to be conveyed.

7. AEC shall also be responsible for a pro rata portion of all cost of making capital improvements and additions, operation, maintenance and decommissioning of the nuclear plant as well as the acquisition of nuclear fuel for such plant, all as more explicitly dealt with in the Operating Agreement.

8. AEC shall waive the rights to partition, or sale in lieu of partition, normally associated with joint ownership of property under Alabama law. In addition, it shall waive all other rights which are normal incidents of joint ownership at common law. AEC's rights as joint owner shall be limited to those expressly stated in the sales contract and operating agreement.

9. AEC shall not have the right to assign, sublet, sell or otherwise dispose of the jointly owned property since to do so could place APCO at additional risk. In the event AEC desires to dispose of its interest in the plant, a mechanism will be developed to give APCO the right, at its election, to purchase AEC's interest in the plant, and establish the price for such transfer.

10. AEC shall indemnify APCO against the adverse impact on APCO arising from tax legislation, or interpretation of tax laws, which impact would arise because of the joint ownership arrangement, i.e., as a result of either the sales agreement or the operating agreement.

B. Operating Agreement:

APCO and AEC shall enter into an Operating Agreement for the operation by APCO of the jointly owned plant. The Operating Agreement shall grant AEC the right to receive its pro rata portion of the energy generated at the plant at the time such generation occurs; however, it shall provide complete and absolute authority in APCO to determine the total operations of the plant, without responsibility on the part of APCO to consult with, or seek agreement of, AEC as to the plant operations, its maintenance, the making of capital improvements, its level of operations, its cessation of operations or the timing or methods of its decommissioning. The Agreement shall provide for the payment, at a minimum, of the costs and fees set forth below.

1. Responsibility of APCO, as Operator, to AEC - Sharing of Costs - Allocation of Risk of Loss of Plant and Damage or Injury to Third Parties.

(a) AEC shall pay, in advance, a pro rata share of all costs associated with operating and maintaining the plant, making capital improvements and additions, acquiring nuclear fuel, participation in nuclear industry organizations determined by APCO to be in the interest of the plant, and for an allocation of general corporate expenses (including but not limited to administrative and general expenses and general plant costs). These obligations shall continue regardless of plant performance or periods of prolonged outage or permanent shutdown. AEC shall agree to accept the terms and conditions of, and agree to be bound by, all contracts associated with construction, operation and maintenance of the plant or the acquisition of nuclear fuel which APCO or others on APCO's behalf have entered into prior to a sale to AEC or which are entered into thereafter. The costs to be shared by AEC shall be those required by regulatory bodies or determined by APCO (in its sole judgment) to be desirable. APCO shall have no liability to AEC for costs of any nature associated with the decision to make such alterations or improvements or to incur such operating or maintenance expense. AEC shall contribute funds in advance from time to time, necessary to acquire nuclear fuel (or its ingredients) during the fuel cycle. Such payments shall be on a pro rata basis. AEC will not be granted title to the fuel or its ingredients but will have contract rights and obligations resulting from such payments.

(b) Fees for operating and maintaining the plant, shall be $1.0 million per year, escalated each year based on an acceptable Government index. A fee shall also be assessed equal to 15% of AEC's pro rata share of all direct and indirect expenditures associated with the making of any capital improvements. A fee equal to ten percent (10%) of AEC's pro rata share of the annual fuel costs shall also be assessed. These

fees have been set on the assumption that APCO will have no responsibility to AEC for any loss associated with the plant, arising out of operations, maintenance, making of improvements or nuclear fuel acquisition activities.

(c) AEC shall be responsible for the total cost of all incremental operating, maintenance, capital improvements or nuclear fuel acquisition activities which result from AEC's ownership interest and which would not have been incurred except for AEC's acquisition of an interest.

(d) AEC shall defend and indemnify APCO for a pro rata portion of costs associated with third party claims arising out of operation of the plant by APCO and for all costs resulting from claims of third parties (such as, claims of AEC's members or customers) which would arise because of AEC's ownership of a portion of the plant.

(e) Provision will be included to exclude liability on the part of APCO for losses or costs to AEC for conduct of APCO, its agents, contractors or employees even though such conduct is alleged or determined to be willful, wanton, reckless or merely negligent.

(f) Provision will be included which will exclude, in any circumstance, liability of APCO to AEC for damages of any nature including those in the character of consequential, special, incidental or indirect damages.

(g) AEC shall be responsible for a pro rata share of all costs associated with the decommissioning of the facilities and disposal of nuclear fuel in accordance with requirements of laws, regulations or mandates of regulatory bodies, and any other costs necessary or desirable, in APCO's sole judgment, for the restoration of the site at the time of the shut-down of the plant. Provisions shall be included in the Operating Agreement to assure that APCO does not incur any additional risk for decommissioning or nuclear fuel waste disposal associated with AEC's interest in the plant.

(h) AEC shall be responsible for a pro rata share of all fines or penalties of any nature, under any law or regulation, associated with the operation, maintenance or decommissioning of the plant, including those imposed by NRC, EPA, other federal, state or local regulatory bodies, or by federal, state or local courts.

(i) The Operating Agreement shall continue in effect until such time that (1) all decommissioning associated with the plant has been completed, (2) all liability for disposal of waste produced or created by the plant has terminated, and (3) the plant site has been returned to a condition acceptable to APCO after decommissioning.

2. Insurance - Liability and Property coverages.

(a) APCO will procure insurance to the extent determined appropriate by APCO (from companies chosen by APCO and under standard policies for such purposes) to cover property damage and public liability (both general liability and nuclear energy hazard insurance). AEC shall bear its pro rata portion of such insurance costs. Such insurance may require AEC to become a member of one or more of the insurance pools in which APCO is a member, such as Nuclear Mutual Limited. APCO shall, in its sole judgment, determine the amount of deductible which will be maintained on insurance.

(b) Mechanisms must be developed to protect against AEC's failure to come up with its pro rata portion of any self-insurance under public liability policies and the Price-Anderson Act.

(c) Similar mechanisms shall be developed to protect against inability or failure of AEC to come up with any retrospective premium adjustments under insurance policies, deductible under property insurance or excess over property insurance necessary to cover entire loss.

(d) In the event it is necessary for AEC to procure insurance associated with replacement power

costs during prolonged outage in order for APCO to be able to maintain such insurance without any increase in cost, then procurement of such insurance by AEC shall be a prerequisite.

3. Failure to Live up to Agreement - Definition and Consequences of Default.

(a) Events of default:

(1) Failure to fund pro rata portion of capital expenditures for improvements, replacements, fuel, etc. Delay in funding that can result in delays in accomplishing the improvement of the plant or the purchase of fuel.

(2) Failure to contribute to working capital fund with sufficient amounts necessary to cover obligations for expenses.

(3) Failure to fund insurance under Price-Anderson.

(4) Failure to provide pro rata share of any retrospective premium adjustments under insurance policies, deductible under property insurance or excess over property insurance necessary to cover entire loss.

(5) Failure to indemnify as required.

(6) Failure to make any other monetary payment when due under the Agreement.

(7) Failure to abide by the requirements of regulatory bodies having jurisdiction over the plant.

(8) Failure to provide adequate assurance of performance by AEC of future obligations where reasonable grounds for insecurity arise.

(9) Disclosure of information which is proprietary to APCO, its suppliers, contractors or agents.

(10) Requirement by APCO, because of court decision, regulatory order or otherwise, to bear more than its pro rata share of the total cost or expense associated with the plant, or which increases APCO's risk, such as, refusal of a court to enforce AEC's obligation to reimburse APCO for fines and penalties of any nature.

(11) Delay by AEC in performance of any action required under the Agreement.

(b) Range of Remedies for Default - Remedies Shall Be Cumulative and not Exclusive of Other Remedies Which May Be Provided by Law.

(1) In any event of default by AEC, it shall be denied its pro rata share of capacity and energy from the plant during continuation of default. APCO shall have the right to sell or use energy from AEC's portion of the plant. AEC would buy replacement capacity and energy at APCO's incremental costs or obtain it from other sources.

(2) AEC would be obligated to pay interest on any monetary amount in default until the default is cured.

(3) AEC shall pay all incremental costs attributable to its default, such as, APCO's replacement power costs resulting from delay.

(4) If a default is not cured within 90 days, APCO would have option to purchase AEC's interest in the plant at AEC's cost less depreciation, less additional costs associated with AEC's default and less APCO's costs associated with transfer and any amounts owed by AEC to APCO. For defaults of the character described in Paragraph B.3(a)(10) above, no period of cure shall be allowed.

(5) In addition to, or in lieu of, right to purchase, APCO would have the right to collect amounts owed, in the past or in the future, by AEC under the Agreement from distribution cooperative members of AEC. Such entities shall enter into contracts which obligate these entities to assume liability for such amounts on a joint and several basis.

(6) REA shall guarantee the contingent liabilities of AEC associated with its ownership interest in the nuclear plant and its responsibility for payment of costs and expenses under the Operating Agreement.

(7) AEC's obligations under the Agreement shall be secured by a second mortgage on AEC's system.

We would note further that in view of our offer made in this letter, we are hereby withdrawing our offer made in 1974 to negotiate the sale of unit power to AEC from the nuclear plant.

Arrangements will be made for our meeting at 9:00 A.M. on May 24, 1983 in the Sixth Floor Conference Room at APCO's General Office Building. We would appreciate your advising us in advance of the representatives you expect to be attending.

Respectfully,

H. Allen Franklin

HAF/iw
Attachments

CONFIDENTIAL

EXHIBIT I

AEC PAYMENTS TO APCO AT CLOSING [a]
(Closing Assumed 6/30/83)
(In Thousands of Dollars)

1.	Estimated Reasonable Value of the Plant [b]	2,965,000
2.	APCO's Costs Related to the Plant [c]	2,430,047
3.	Average of Items 1 and 2	2,697,524
4.	Nuclear Fuel Costs [d]	303,885
5.	Total for 100% of Units	3,001,409
6.	Sub-Total to be Paid by AEC @ 5.95% Ownership Interest [e]	178,584
7.	Adjustment: Transfer of Ownership Costs [f]	
8.	Total to be Paid by AEC (Item 6 plus Item 7)	

NOTES:

(a) Data to be revised and adjusted to actual closing date. Cost estimates rounded to nearest 1,000 dollars.

(b) EBASCO Services, Incorporated estimate of reproduction cost less depreciation.

(c) Details of these costs are on Exhibit I, page 2.

(d) Details of these costs are on Exhibit I, page 3.

(e) This price will be adjusted for any unforeseen adverse tax impacts.

(f) Transfer of ownership costs include filing and recording fees, proration of certain taxes, proration of certain prepaid items, APCO cost of negotiating and implementing sales/operating agreements, etc. (to be determined based on actual transaction costs).

EXHIBIT I

APCO'S COSTS RELATED TO THE FARLEY NUCLEAR PLANT [a]
(Closing Assumed 6/30/83)
(In Thousands of Dollars)

Net Adjusted Investment @ 6/30/83	1,420,721
Capital costs during construction in excess of booked	463,328
Adjustment for Income Tax Effect [b]	245,656
Entitlement Fee [c]	170,071
Other adverse financial consequences associated with building Plant Farley	114,200
Construction Work in Progress	16,071
TOTAL	2,430,047

NOTES:

(a) Data to be revised and adjusted to actual closing date. Cost estimates rounded to nearest 1,000 dollars.

(b) The estimated income tax effect will be actualized to reflect any unforeseen adverse impact.

(c) "Entitlement Fee" is an amount to be paid by AEC in consideration of construction planning, construction management, plant design, labor supervision, site licensing, use of a valuable scarce site, and AEC's entitlement to the Company's contracts for major equipment.

EXHIBIT I

NUCLEAR FUEL COSTS (a)
(Closing Assumed 6/30/83)
(In Thousands of Dollars)

Net Adjusted Investment	78,119
Capital costs during fabrication in excess of booked	45,704
Adjustment for Income Tax Effect (b)	8,915
Construction Work in Progress	171,147
TOTAL	303,885

NOTES:

(a) Data to be revised and adjusted to actual closing date. Cost estimates rounded to nearest 1,000 dollars.

(b) The estimated income tax effect will be actualized to reflect any unforeseen adverse impact.

ATTACHMENT 4

ATTACHMENT 4

AEC PAYMENTS TO APCO AT CLOSING[a]
(Closing Assumed 6/30/83)

		$000	$/kw
1.	Estimated Reasonable Value of the Plant[b]	2,965,000	1,724
2.	APCO's Costs Related to the Plant[c]	2,430,047	1,413
3.	Average of Items 1 and 2	2,697,524	1,568
4.	Nuclear Fuel Costs[d]	303,885	177
5.	Total for 100% of Units	3,001,409	1,745
6.	Sub-Total to be Paid by AEC @ 6.26% Ownership Interest[e]	187,888	1,745
7.	Adjustment: Transfer of Ownership Costs[f]		
8.	Total to be Paid by AEC (Item 6 plus Item 7)		

NOTES:

(a) Data to be revised and adjusted to actual closing date. Cost estimates rounded to nearest 1,000 dollars.

(b) EBASCO Services, Incorporated estimate of reproduction cost less depreciation.

(c) Details of these costs are on Attachment 4, page 2.

(d) Details of these costs are on Attachment 4, page 3.

(e) This price will be adjusted for any unforeseen adverse tax impacts.

(f) Transfer of ownership costs include filing and recording fees, proration of certain taxes, proration of certain prepaid items, APCO cost of negotiating and implementing sales/operating agreements, etc. (to be determined based on actual transaction costs).

ATTACHMENT 4 (Continued)

APCO'S COST RELATED TO THE FARLEY NUCLEAR PLANT[a]
(Closing Assumed 6/30/83)

	$000	$/kw
Net Adjusted Investment @ 6/30/83	1,420,721	826
Capital Costs during construction in excess of booked	463,328	269
Adjustment for Income Tax Effect[b]	245,656	143
Entitlement Fee[c]	170,071	99
Other adverse financial consequences associated with building Plant Farley	114,200	66
Construction Work in Progress	16,071	9
TOTAL FOR 100% OF PLANT	2,430,047	1,413

NOTES:

(a) Data to be revised and adjusted to actual closing date. Cost estimates rounded to nearest 1,000 dollars.

(b) The estimated income tax effect will be actualized to reflect any unforeseen adverse impact.

(c) "Entitlement Fee" is an amount to be paid by AEC in consideration of construction planning, construction management, plant design, labor supervision, site licensing, use of a valuable scarce site, and AEC's entitlement to the Company's contracts for major equipment.

ATTACHMENT 4 (Continued)

NUCLEAR FUEL COSTS[a]
(Closing Assumed 6/30/83)

	$000	$/kw
Net Adjusted Investment	78,119	45
Capital costs during fabrication in excess of booked	45,704	27
Adjustment for Income Tax Effect[b]	8,915	5
Construction Work in Progress	171,147	100
TOTAL FOR 100% OF FUEL	303,885	177

NOTES:

(a) Data to be revised and adjusted to actual closing data. Cost estimates rounded to nearest 1,000 dollars.

(b) The estimated income tax effect will be actualized to reflect any unforeseen adverse impact.

ATTACHMENT 5

ALABAMA POWER COMPANY

FARLEY NUCLEAR GENERATING STATION

REPLACEMENT COST STUDY

EBASCO SERVICES INCORPORATED

MARCH, 1983

ALABAMA POWER COMPANY

FARLEY NGS REPLACEMENT COST STUDY

Introduction/Results

Alabama Power Company authorized Ebasco Services Incorporated to provide generic capital cost estimates for two 860 MW PWR nuclear units in the state of Alabama to determine a replacement cost for the Farley Nuclear Generating Station. Based on the generic estimates, the depreciated replacement cost of the Farley NGS could be determined. The study also provides a generic impact assessment of schedule delays which have normally impacted nuclear plant construction, generally, due to changing regulatory guidelines.

The following table summarizes the estimates prepared:

REPLACEMENT COST ESTIMATES - $ x (1000)

Base Case (No Delay)	C.O. Date	Replacement Cost	Replacement Cost Less Depreciation
Unit 1	7/83	1,812,000	1,524,000
Unit 2	7/83	1,535,000	1,441,000

DELAY SCENARIO'S

REPLACEMENT COST ESTIMATE-$ x (1000)

2 year delay (No Scope Change)	C.O. Date	Cost at C. O. Date	Cost Discounted to 7/83*
Unit 1	7/85	2,298,000	1,970,000
Unit 2	7/85	1,950,000	1,672,000
2 year delay (With Scope Change)			
Unit 1	7/85	2,484,000	2,130,000
Unit 2	7/85	2,070,000	1,775,000
4 year delay (No Scope Change)			
Unit 1	7/87	2,900,000	2,132,000
Unit 2	7/87	2,440,000	1,793,000

Base Case (No Delay)	C. O. Date	Replacement Cost	Replacement Cost Less Depreciation
4 year delay (With Scope Change)			
Unit 1	7/87	3,350,000	2,462,000
Unit 2	7/87	2,730,000	2,007,000

*at assumed 8% rate of escalation per annum

METHODOLOGY

The scope of work performed by Ebasco for this study consisted of developing generic capital investment estimates for two 860MW PWR nuclear units constructed in the State of Alabama based on 1983 regulatory requirements and a generic schedule assuming no delays. The construction schedule for the generic two unit plant assumes the units will be built sequentially with two years between the commercial operation dates of the units. No cost penalty has been provided in assuming both units are to be placed into commercial operation on the same date of July 1, 1983. In order to provide the Unit 1 and Unit 2 estimates on the same C.O. date, without a construction cost penalty, Ebasco assumed two identical 2-unit plants were being constructed. These two plants were further assumed to have identical schedules and design requirements with one plant having a July, 1983 C.O. for Unit 1 while the other plant has a July 1983 C.O. for Unit 2.

The construction schedule for the identical unit (Unit #1) assumes a six month duration for site mobilization and site preparation before the first placement of concrete and six month duration between fuel load and commercial operation. The overall project schedule assumes a 48 month licensing and engineering duration prior to issuance of the construction permit, and 75 month construction duration to commercial operation of Unit #1.

The extension unit (Unit #2) is assumed to be licensed, engineered, and constructed sequentially with unit #1 and assumes a 69 month constuction period from first concrete to commercial operation. The initial unit is assumed to begin licensing in 1973 in order to attain a July, 1983 C.O. date. The extension unit (Unit #2) of a sequentially constructed two unit plant would begin licensing in 1971 to meet a 1983 C.O. date for the second unit. Exhibit 1 illustrates the assumed generic construction schedules utilized as the basis of the replacement cost analysis.

The estimates include a pressurized water reactor designed and constructed according to the regulatory guides and standards set by the U.S. Nuclear Regulatory Commission as of January, 1983. A flat level site is assumed with common facilities for both units included in the cost of Unit #1.

Included in the cost is the complete unit design, construction, testing, approval and readiness for a July 1983 Commercial Operation.

The plants' scope includes enclosed turbine buildings, natural draft cooling towers, full radwaste handling and treatment facilities, all safety and security provisions and all supporting structures, systems, and services. The cost of the following are excluded from the estimates:

a) Land and land rights

b) Transmission lines

c) Fuel

d) Operator training

e) Client administrative and other client charges

f) Regulatory guides pending after January, 1983

g) Decommissioning Cost

The estimates were prepared on the basis of Ebasco's data and experience on other nuclear projects and assumes the availability of material and equipment based on lead times that were expected during the assumed construction period and the availability of manual and non-manual personnel in the numbers and skills required for construction. The investment estimates were developed based on the cost of (2) 860 MW PWR units in 1983 constant or instantaneous dollars excluding AFUDC. Based on the generic construction schedules a cash flow of capital expenditures for both units was developed and the investment de-escalated to the anticipated year of expenditure. Ebasco's historical material composite index for nuclear plants, a compilation of cost increases for the NSSS package, the turbine-generator, other equipment, and bulk commodities was utilized to adjust the material and equipment component to the de-escalated point of expenditure. The installation component was developed based on the R.S. Means historical labor indices in the State of Alabama and also de-escalated to the anticipated point of expenditure. The average wage rates for Birmingham, Alabama were utilized in the analysis since they are representative of labor costs in Alabama based on a review of four cities, Birmingham, Gadsden, Huntsville, and Montgomery.

Exhibit 2 illustrates Ebasco's material composite index for nuclear units and the installation component based on Birmingham, Alabama craft wage rates. An overall material and installation composite index was then computed based on a 60%/40% material to installation weighted average.

The material index indicates the average real cost increases for material and equipment components in a nuclear plant facility for the past thirteen years. The installation component indicates the average real cost increases in the Birmingham, Alabama area for craft labor.

The composite material and installation index is the weighted average based on this 60%/40% material to labor percentage.

Exhibit 3 and 4 illustrate the adjustments made to de-escalate the 1983 constant dollar estimates to the cash flow expenditure pattern assumed for the construction of Unit #1 and Unit #2. These estimates are considered the base case in our analyses with all milestones in the construction schedule met and no delay in any phase of the construction period. Exhibit 5 indicates a major component breakdown of the capital cost estimates for an assumed July, 1983 C.O. date with AFUDC. The de-escalated cash flows in Exhibits 3 & 4 were utilized to compute AFUDC. The period considered is from 1971 to July 1, 1983. The interest rates used in the computation are shown below and Exhibit 6, a historical curve of long term bond yields.

YEAR	AVERAGE Baa INTEREST RATES USED (%)
1971	8.5
1972	8.5
1973	8.0
1974	9.5
1975	11.0
1976	10.0
1977	9.0
1978	9.5
1979	11.0
1980	13.5
1981	16.5
1982	17.0
1983	15.0

As indicated in Exhibit 6, the period from 1971 through 1983 was a period of volatile interest rates, so an average rate was developed for each year. Although using long term bond yields to estimate the cost of construction is not entirely correct it is felt that it is an approximation which is within the accuracy of the capital cost estimate. A more detailed examination would require an analysis of the financial position of the company, the proportion of debt and equity used for construction financing, and the sources for these funds. Such an analysis is beyond the scope of this study. Exhibits 7 and 8 summarize the base case capital cost estimates with AFUDC included.

The depreciated replacement cost was than calculated based on the following data provided by Alabama Power Company:

	Economic Life	Life Expended on 7/1/83	Remaining Life
Farley Unit #1	35 yrs. 1 mos	5 yrs. 7 mos.	29 yrs. 6 mos
#2	31 yrs. 5 mos	1 yr. 11 mos	29 yrs. 6 mos

The following were the results of the analysis for the base case assuming straight line depreciation with no decommissioning costs included.

REPLACEMENT COST LESS DEPRECIATION - $ x (1000)

Unit 1	1,524,000
Unit 2	1,441,000

Using the cash flows developed from the base case, four delay scenarios were analyzed and their impact on the construction costs. It was assumed that the scheduled delays would occur one year before the scheduled fuel loading of the units. Exhibits 9 and 10 illustrate the effect of construction delays on the base plant costs with and without any additional expenditures due to scope changes included in the project. It was assumed for purposes of illustration that an additional 5% of the plant cost would be incurred at each delay point for the scenarios where expenditures for scope changes are considered.

In developing these four scenarios, an 8% escalation rate per year and a 12% interest rate was utilized beyond July, 1983. The four delay scenarios are:

1) 2 year delay without a project scope change.

2) 2 year delay with a project scope change

3) 4 year delay without a project scope change

4) 4 year delay with a project scope change

ALABAMA POWER COMPANY

FARLEY N.G.S. REPLACEMENT COST STUDY
CONSTRUCTION SCHEDULE - BASE CASE

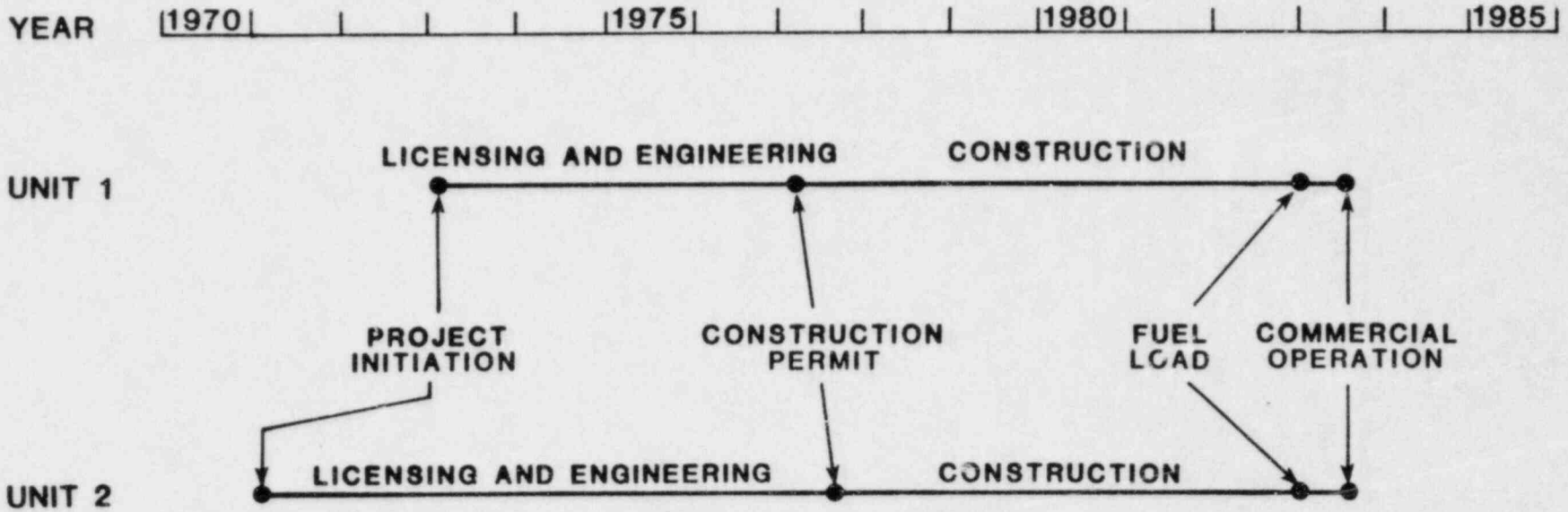


EXHIBIT 1

EXHIBIT 2

ALABAMA POWER COMPANY

FARLEY N.G.S. REPLACEMENT COST STUDY

MONTH/YEAR	EBASCO'S MATERIAL COMPOSITE INDEX	COMPOSITE WAGE INDEX BIRMINGHAM	*COMPOSITE MATERIAL AND INSTALLATION MULTIPLIER
6-71	.323	.397	.350
6-72	.350	.428	.380
6-73	.368	.463	.404
6-74	.446	.500	.467
6-75	.501	.540	.516
6-76	.544	.583	.559
6-77	.589	.630	.603
6-78	.649	.680	.661
6-79	.719	.735	.720
6-80	.801	.793	.797
6-81	.879	.857	.869
6-82	.954	.925	.942
1-83	1.000	1.000	1.000

*Based on a 60%/40% split between material and installation.

ALABAMA POWER COMPANY

FARLEY N.G.S. REPLACEMENT COST STUDY

UNIT #1 - BASE CASE - NO DELAY IN CONSTRUCTION

YEAR OF EXPENDITURE	1983 $(x 1000) (CONSTANT DOLLARS)	COMPOSITE MATERIAL AND INSTALLATION MULTIPLIER	TOTAL $(1000)
1973	17,100	.404	7,000
1974	19,270	.467	9,000
1975	35,850	.516	18,500
1976	55,470	.559	31,000
1977	134,610	.603	81,100
1978	340,300	.661	224,900
1979	363,570	.720	262,900
1980	275,680	.797	219,700
1981	143,170	.869	124,200
1982	52,680	.942	49,600
1983	9,300	1.000	9,300
	1,447,000		1,037,200

EXHIBIT 4

ALABAMA POWER COMPANY

FARLEY N.G.S. REPLACEMENT COST STUDY

UNIT #2 - BASE CASE - NO DELAY IN CONSTRUCTION

YEAR OF EXPENDITURE	1983 $ x(1000) (CONSTANT DOLLARS)	COMPOSITE MATERIAL AND INSTALLATION ADJUSTMENT	TOTAL $(1000)
1971	5,600	.350	2,000
1972	5,600	.380	2,000
1973	7,500	.404	3,000
1974	8,700	.467	4,000
1975	24,550	.516	12,500
1976	43,580	.559	24,000
1977	110,150	.603	66,400
1978	302,630	.661	200,000
1979	317,130	.720	228,300
1980	236,020	.797	188,100
1981	117,680	.869	101,200
1982	42,260	.942	39,600
1983	7,600	1.000	7,600
TOTAL:	1,229,000		878,700

EXHIBIT 5

ALABAMA POWER COMPANY

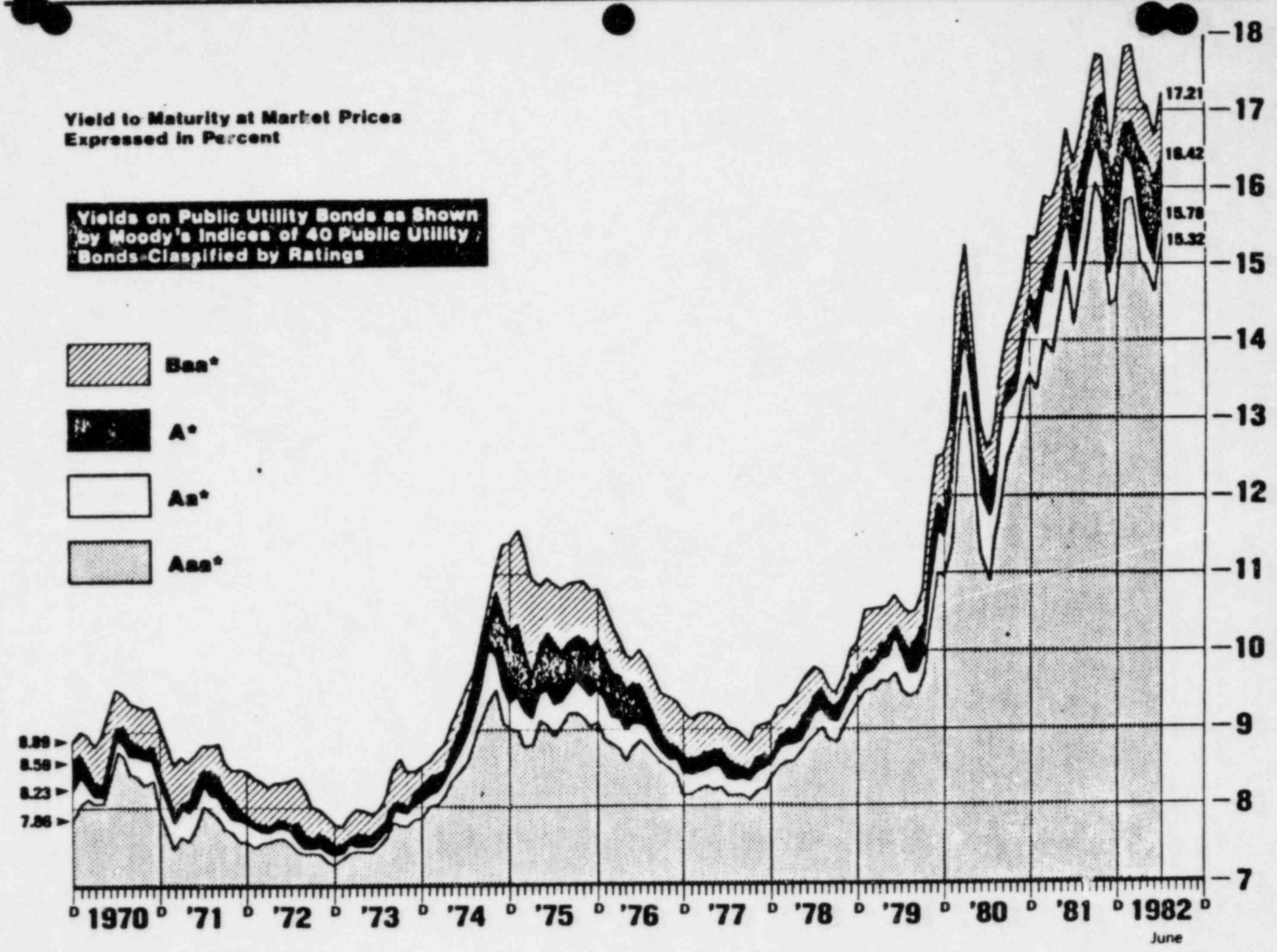
FARLEY N.G.S. REPLACEMENT COST STUDY

CAPITAL INVESTMEMT ESTIMATE-BASE CASE

UNIT #1 1983 C.O.	$ x (1000)
Nuclear Steam Supply System	72,000
Turbine-Generator	48,000
Civil Work	240,000
Balance of Plant	677,200
Total Construction Cost (1983 C.O. Without AFUDC)	1,037,200

UNIT #2 1983 C.O.	
Nuclear Steam Supply System	72,000
Turbine Generator	48,000
Civil Work	220,000
Balance of Plant	538,700
Total Construction Cost (1983 C.O. Without AFUDC)	878,700

YIELDS ON PUBLIC UTILITY BONDS



*Ten Public Utilities

Source: Moody's

EBASCO

ALABAMA POWER COMPANY
FARLEY N.G.S. REPLACEMENT COST STUDY

EXHIBIT 6

EXHIBIT 7

ALABAMA POWER COMPANY

FARLEY N.G.S. REPLACEMENT COST STUDY

UNIT #1 - BASE CASE - NO DELAY IN CONSTRUCTION

$ x (1000)

YEAR OF EXPENDITURE	TOTAL COST WITHOUT AFUDC	AFUDC	TOTAL COST WITH AFUDC
1973	7,000	300	7,300
1974	9,000	1,100	10,100
1975	18,500	2,900	21,400
1976	31,000	5,400	36,400
1977	81,100	10,400	91,500
1978	224,900	26,500	251,400
1979	262,900	60,400	323,300
1980	219,700	114,900	334,600
1981	124,200	187,800	312,000
1982	49,600	240,200	289,800
1983	9,300	124,900	134,200
TOTAL	1,037,200	774,800	1,812,000

ALABAMA POWER COMPANY

FARLEY N.G.S. REPLACEMENT COST STUDY

UNIT #2 - BASE CASE - NO DELAY IN CONSTRUCTION

$ x (1000)

YEAR OF EXPENDITURE	TOTAL COST WITHOUT AFUDC	AFUDC	TOTAL COST WITH AFUDC
1971	2,000	100	2,100
1972	2,000	300	2,300
1973	3,000	470	3,470
1974	4,000	940	4,940
1975	12,500	2,100	14,600
1976	24,000	3,940	27,940
1977	66,400	8,000	74,400
1978	200,000	21,800	221,800
1979	228,300	51,300	279,600
1980	188,100	97,900	286,000
1981	101,200	159,700	260,900
1982	39,600	203,700	243,300
1983	7,600	106,050	113,650
TOTAL	878,700	656,300	1,535,000

ALABAMA POWER COMPANY

FARLEY N.G.S. REPLACEMENT COST STUDY

UNIT #1

	YEAR OF C.O.	TOTAL PLANT COST ($1 x 1000)	% INCREASE
Base Case	1983	1,812,000	Base
Two year delay No additional funds expended	1985	2,298,000	26.8
Two year delay 5% of expenditures made one year before fuel loading at each delay	1985	2,484,000	37.0
Four year delay No additional funds expended	1987	2,900,000	60.0
Four year delay 5% of expenditures made one year before fuel loading at each delay	1987	3,350,000	84.9

EXHIBIT 10

ALABAMA POWER COMPANY

FARLEY N.G.S. REPLACEMENT COST STUDY

UNIT #2

	YEAR OF C.O.	TOTAL PLANT COST ($ x 1000)	% INCREASE
Base Case	1983	1,535,000	Base
Two year delay	1985	1,950,000	27.0
No additional funds expended			
Two year delay	1985	2,070,000	34.8
5% of expenditures made one year before fuel loading at each delay			
Four year delay	1987	2,440,000	58.9
No additional funds expended			
Four year delay	1987	2,730,000	77.9
5% of expenditures made one year before fuel loading at each delay			

ATTACHMENT 6

ATTACHMENT 6
COMPARISON OF NUCLEAR UNIT CAPITAL COSTS
ESTIMATES OF
EBASCO'S REPLACEMENT COST - UNIT 1
vs.
NUCLEAR UNITS NOW UNDER CONSTRUCTION

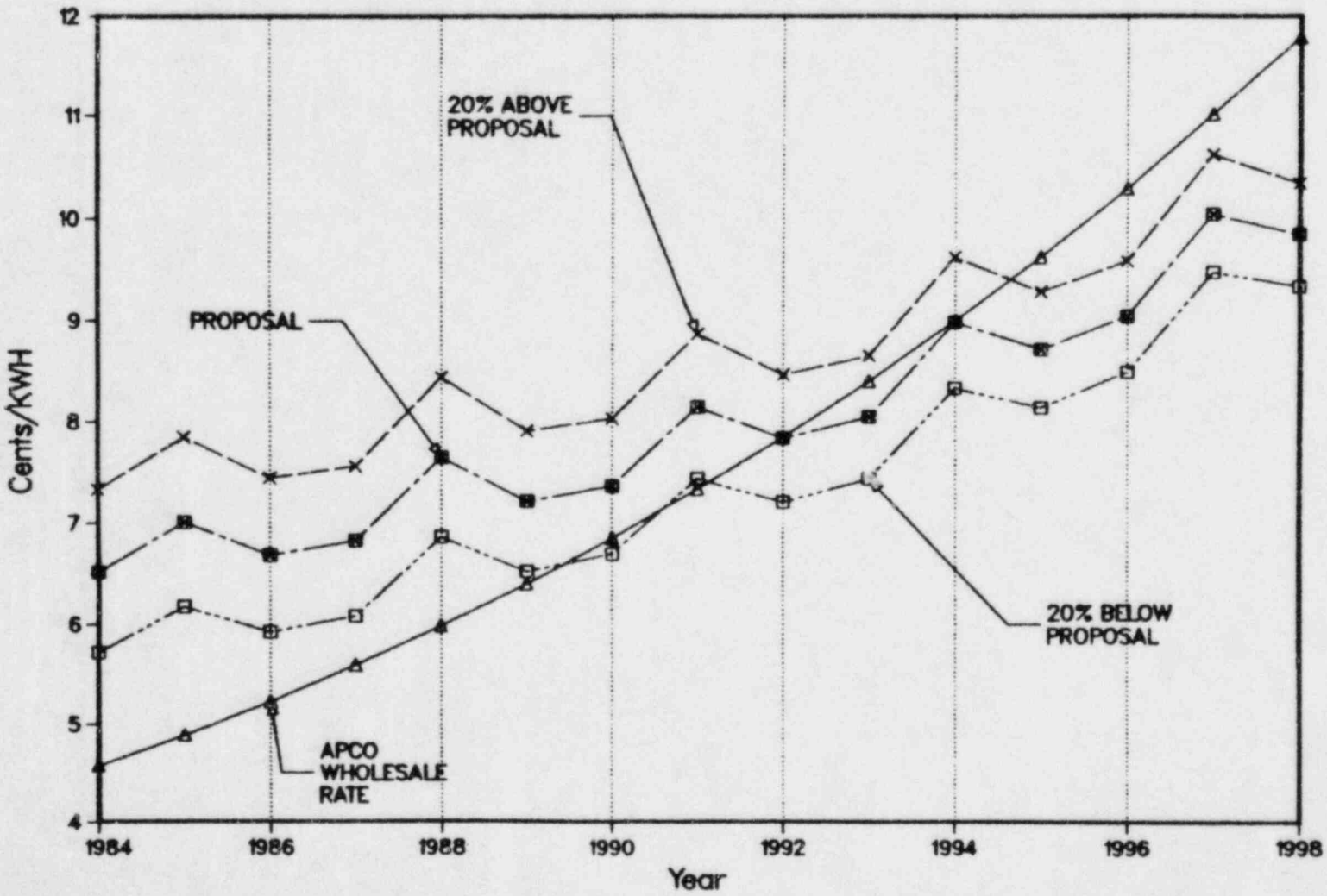
		$/kW Without AFUDC 1983 Constant Dollars	
Rank	Unit	Estimate of[1] Units Now Under Construction	EBASCO's Unit 1 Estimate
1	Diablo Canyon 1	1331	
2	Braidwood 1	1399	
3	Catawba 1	1400	
4	LaSalle 1	1463	
5	Marble Hill 1	1482	
6	Palo Verde 1	1657	1683[2]
7	Byron 1	1713	
8	Summer	1731	
9	Bellefonte 1	1756	
10	Wolf Creek	1781	
11	Watts Bar 1	1808	
12	St. Lucie 2	1914	
13	Seabrook 1	2061	
14	Waterford 3	2100	
15	Perry 1	2130	
16	WNP-2	2170	
17	Limerick 1	2191	
18	Callaway 1	2222	
19	Harris 1	2269	
20	Susquehanna 1	2309	
21	Zimmer	2331	
22	Clinton 1	2350	
23	San Onofre 2	2400	
24	Millstone 3	2570	
25	Nine Mile Point 2	2600	
26	Fermi - 2	2676	
27	Midland 2	2734	
28	Beaver Valley 2	2753	
	Limerick 1	2808	
29	Hope Creek 1	3028	
30	Vogtle 1	3348	
31	Shoreham	4160	

[1] SOURCE: Based on data presented in United Engineers and Construction Inc., Analysis of Nuclear Power Plant Costs Submitted on DOE Form 254, Presentation Materials, Philadelphia, Pennsylvania, August, 1983. Cost shown reflects estimates as of December, 1982.

2 "Farley Nuclear Generating Station Replacement Cost Study," EBASCO, March 1983.

ATTACHMENT 7

WHOLESALE VS. OWNERSHIP COST OF POWER



Alabama Power Company
600 North 18th Street
Post Office Box 2641
Birmingham, Alabama 35291
Telephone 205 250-1000

August 28, 1984

Mr. Charles R. Lowman
General Manager
Alabama Electric Cooperative, Inc.
P. O. Box 550
Andalusia, Alabama 36420

Dear Charles:

In recent months, we have been involved in discussions with the Southeastern Power Administration (SEPA) concerning revisions in arrangements for the sale of wholesale power by SEPA to its "preference customers" in Alabama, and the transmission of such power to SEPA's customers. These customers, of course, include distribution cooperatives which are members of AEC and which have appointed AEC as their power supply agent. Included are: (a) cooperatives which purchase from Alabama Power all of their requirements, other than purchases from SEPA, and (b) cooperatives which purchase from AEC all of their requirements other than purchases from SEPA, all of which power is transmitted over Alabama Power's transmission lines. You have already advised us that certain customers now in category (a) will be transferred to category (b) within the next year.

Our discussions with SEPA have proceeded on the assumption that Alabama Power would have the opportunity to schedule the SEPA capacity which is allocated to cooperatives in category (a). Alabama Power, in effect, firms up this capacity in return for which all customers of Alabama Power share the benefits from the scheduling of SEPA capacity. As a part of this total package of benefits and costs, Alabama Power will be agreeing, for the first five years of the new arrangement, to compensation for transmission service which is less than the total costs for performing the SEPA power transmission function.

Cooperatives in category (b), including those which AEC moves from category (a) to category (b) during the next ten years, are covered by the Agreement for Transmission Service between Alabama Power and AEC. Paragraph 3.C.(3) of that Agreement provides for revision of the Transmission Agreement if the character of the SEPA allocation changes. The changes

which have been suggested by SEPA are of a substantially different character; however, we feel that the method of accounting for SEPA under the present Transmission Agreement can remain in place.

AEC has, on numerous occasions, suggested that it be given authority to schedule the SEPA capacity allocated to these category (b) cooperatives any way it wishes - just as if this SEPA capacity were another resource of AEC for meeting its wholesale power responsibility. We have suggested that the new SEPA contract reflect such desire of AEC. Representatives of SEPA have stated that, in conversations with you, AEC has disclaimed any desire to have the total load of these wholesale customers treated as a load of AEC. Rather, according to SEPA, AEC wanted SEPA to have the responsibility, in conjunction with Alabama Power's services, to carry that portion of the loads of the category (b) cooperatives with Alabama Power retaining the right to schedule this capacity. We wish for you to confirm this in writing.

In the alternative, we have told SEPA that we are willing for the SEPA capacity allocated to the category (b) cooperatives to be scheduled by AEC just as any other resource of AEC used to serve the total load of these wholesale customers. Under this alternative, the allocation to category (b) cooperatives would not be included in the Alabama Power-SEPA contract, but power supply for those cooperatives would be furnished by AEC over Alabama Power's transmission facilities pursuant to the Transmission Agreement.

In any event, we have told SEPA that we are concerned over entering into the arrangement which SEPA has proposed unless it were clear from the outset that the preference customers and their power supply agent did not claim such an arrangement to violate the antitrust laws or somehow be inconsistent with such laws. We, therefore, request that you notify us immediately whether AEC:

1. Elects for the loads served by SEPA capacity allocated to category (b) cooperatives to be considered loads of SEPA with the capacity being subject to scheduling by Alabama Power; or

2. Elects for the loads served by SEPA capacity allocated to category (b) cooperatives to be considered loads of AEC with the capacity being subject to scheduling by AEC.

We also request that AEC inform us at this time whether it has any objection to Alabama Power's proposed contract with SEPA if such contract is consistent with the alternative selected by AEC.

We need a prompt response in order to consummate an arrangement with SEPA.

Sincerely,

A. J. Connor
General Manager-Electric
System Planning and Power
Contracts

Alabama Electric Cooperative, Inc.
Post Office Box 550
Andalusia, Alabama 36420
(205) 222-2571

Charles R. Lowman
General Manager

AEC

September 4, 1984

Mr. A. G. Connor
General Manager-Electric
System Planning and Power Contracts
Alabama Power Company
Post Office Box 2641
Birmingham, Alabama 35291

Dear Joe:

The savings to AEC members in having category (b) cooperatives (those receiving their power requirements from AEC other than SEPA purchases) covered under the Alabama Power-SEPA contract outweigh any scheduling benefits in having the added SEPA capacity on-system. Therefore, we elect to have SEPA deliver preference power to category (b) cooperatives and continue with the arrangement under the APCo-AEC Transmission Agreement for the next five years until rates for SEPA wheeling become fully cost-based.

While we do not know the complete details of the Southern Company-SEPA tentative agreement, we realize that it is an arrangement involving a number of considerations and we have no objection to the Alabama Power-SEPA contract related to wheeling as long as it provides for the delivery method that we have selected.

Sincerely,

Charles R Lowman

Charles R. Lowman
General Manager

CRL:elf

cc: Mr. Kenelm E. Rucker, SEPA

ATTACHMENT 9

Alabama Power Company
600 North 18th Street
Post Office Box 2641
Birmingham, Alabama 35291
Telephone 205 250-1000

JESSE S. VOGTLE
Executive Vice President

Alabama Power
the southern electric system

September 26, 1983

Mr. Charles R. Lowman
Alabama Electric Cooperative, Inc.
P. O. Box 550
Andalusia, Alabama 36420

Dear Mr. Lowman:

In our meeting on September 1, 1983 we agreed that we would undertake to set forth the status of negotiations being conducted between Alabama Power Company and Alabama Electric Cooperative, Inc. pursuant to Section 2.F(2) of the Operating Licenses for the Joseph M. Farley Nuclear Plant Units 1 and 2. In doing so, we discovered three basic categories of issues which have been raised to date: (1) those as to which the parties are in agreement; (2) those as to which the parties understand the positions and are in agreement in principle but reserve their rights to look at the issue in greater detail as negotiations progress; and (3) those as to which the parties are in fundamental disagreement at the present time. We are identifying and categorizing these issues below.

A. SALE OF [illegible]

1. Amount of Joint Ownership Interest to be Sold to AEC under Section 2.F(2): APCO originally set forth its understanding of the requirements of the license condition which would have resulted in an offer to AEC of 5.95% of the plant, that is, approximately 102 megawatts of nameplate capacity. AEC countered stating its disagreement. No explicit entitlement was specified by AEC, however, from the principles stated in its disagreement with APCO's methodology, AEC appears to be claiming entitlement to approximately 6.75%, or 116 megawatts of nameplate capacity. APCO examined AEC's objections and has agreed that transmission losses in the computation of the demand of AEC off system customers served by APCO were handled inconsistently and

that recalculation based on the available data showed the entitlement to be offered AEC under the license condition should be 6.26%, or 108 megawatts. AEC still maintains that the Appeal Board intended to require division of the plant not just on the ratio of AEC sales to its members compared to total sales of AEC and APCO, but it also wished to increase AEC's share of the plant entitlement based on sales made by Southeastern Power Administration to AEC's members which power was wheeled over APCO's lines to such members.

APCO continues to reject this argument. The Joseph M. Farley Plant was designed in the late 1960's to serve the load in Alabama which APCO was under a duty to serve. Of that expected load no more than 4% was load of distribution cooperatives which are now off system members of AEC. Thus, on the basis of normal allocation methodologies utilized by regulatory bodies, only approximately 4% of the Farley Plant (and the associated costs) would have been available to AEC's members. Even though AEC came into the picture long after plans for the unit had been finalized, AEC argued successfully before NRC that it should be entitled to purchase greater than pro rata share of this resource. The erosion is dramatic. In 1969 when plans were developed for the Farley Plant (including fixing the size of the units) at least 96% of the plant was intended for provision of service to the customers of the company other than those of AEC. When the Licensing Board ordered the APCO to provide unit power access to AEC in 1976, the requirement would have resulted in AEC having an allocation of 5% of the plant. 95% would have been retained for service to APCO's other customers. The Appeal Board's efforts result in the erosion of an additional 1.26% of plant allocation so that only 93.74% is available for service to APCO's customers. Now, AEC wants to go further to expand its interest to nearly 7% leaving slightly more than 93% for APCO's customers. It appears inconsistent for AEC to take the position which it is taking today in light of the representations which were made to the Eleventh Circuit Court of Appeals by counsel for Department of Justice (in the presence of AEC) that the order would result in the sale of approximately 4% to 6% of the plant.

In summary, while APCO has moved from its initial position, AEC has not yet indicated a willingness to budge from its insistence on access to approximately 7% of the plant. In addition to the above, we would note that the figures which have been used in developing the ratios are, in some instances, estimates. This estimation is required because of missing data at some delivery points. We also

would note that AEC has not supplied any back-up for its statement of coincident peak demand of its Alabama wholesale customers.

2. Sales Price: APCO's understanding of the basis for the sales price was set forth in its letter to AEC dated April 29, 1983. AEC has vehemently rejected such basis and has countered stating it would not pay more than what it would have incurred on a computed basis had APCO sold AEC an ownership interest at the time it first sought such an interest. AEC should clearly recognize this as a punitive measure which would permit it access to ownership in the plant significantly below APCO's costs. APCO has rejected that concept and the parties are in fundamental disagreement on this issue.

3. Amount of Real Property Conveyed and Conveyance Mechanism: APCO originally offered to convey by quit claim deed a joint interest in all of the improvements constituting the plant exclusive of the underlying fee in the property except for the fee underlying the ten acre tract comprising the Security Protected Area. AEC objected to a quit claim deed on the basis of REA requirements as lender even though the U.S. Government will not normally convey property other than by quit claim deed. APCO has agreed to convey by statutory warranty deed an ownership interest in all improvements on the plant site which are part of the Farley Plant together with joint ownership in a surface area of approximately 115 acres on which the majority of those facilities constituting the Farley Plant are located. APCO has also offered to include contract provisions which would allow AEC to purchase an interest in any future improvements in Farley Units 1 and 2 without the necessity of purchasing additional property. AEC has agreed to review this proposal for compatibility with REA lending requirements. APCO continues to be concerned with any requirement that it sell an ownership interest in fee simple to portions of the site which are not directly related to the Farley Plant. Unrelated uses which APCO may wish to make of such property should not be encumbered because of principles of joint ownership under which AEC might claim participation rights. APCO has also stipulated that any rights in land conveyed to AEC shall be reconveyed to APCO for nominal considerations after complete decommissioning. AEC has agreed to this reconveyance at a "fair price".

4. Sale of Nuclear Fuel: Because of the complications in the title to nuclear fuel which APCO has leased for financing purposes, APCO originally suggested that it not be

required to convey an ownership interest in the fuel. Rather APCO suggested AEC's interest could be protected through a contract right to a pro rata portion of energy produced by the fuel. AEC objected stating that REA would probably want AEC to have a joint ownership interest in the fuel itself. APCO has investigated the possibility of making the conveyance to accommodate AEC's position and feels that, while it will be time consuming and complicated to straighten out the title situation with APCO's third party lessors, it can probably be done. Some "work out" period may be required, however. While the details of this conveyance have not been fleshed out and are expected to be complex, we do not expect there to be any insurmountable problems conveying a joint ownership interest in existing fuel inventories to AEC. AEC has agreed to explore further whether REA needs title to nuclear fuel as security for loans made to pay for such fuel, or whether some other interest could suffice.

5. Warranties: APCO noted in its original offer that the facilities conveyed to AEC would be conveyed in an "as is, where is basis" with negation of express and implied warranties. AEC has agreed and has submitted a draft provision for that purpose. AEC's clause is an acceptable starting point for development of contract language. Enclosed is a redraft of that clause. You will note that the issue of rights with respect to third party contracts is dealt with in 6 below.

6. Acceptance of Contracts: APCO has requested AEC to accept the terms and conditions of contracts which APCO has entered into, prior to the sale, in connection with the plant construction, operation and maintenance, or the purchase of nuclear fuel or other fuel cycle related contracts. AEC has not expressed objection to this requirement. A clause entitled "Contracts with Third Parties" dealing with these matters as it relates to plant facilities has been developed and is enclosed. A similar clause will be developed for fuel related issues.

7. Incremental Costs Incurred under Third Party Contracts: APCO has proposed, and AEC objected to, recognition of the principles that, if under contracts with third parties relating to the facilities to be conveyed, there results additional costs solely because of the sale of an ownership interest in the plant to AEC, AEC should bear that incremental cost. We are not aware of any actual cases of incremental costs which would result from contracts, but we have difficulty understanding why the principle is

unacceptable to AEC. In this category of potential incremental costs, we are strictly talking about cost items which will be identified by the third party contractor as being imposed solely because of the addition of AEC to an ownership interest. Thus, AEC's concern is unfounded that APCO will attempt to make an improper cost allocation. An example of the type of charge which could be imposed would be a charge for increased insurance premiums incurred by the contractor because of the addition of AEC as an owner, assuming of course, that the contractor has a right to pass on such a charge to APCO pursuant to the contract. We would request AEC to reassess its position on this matter.

8. Incremental Costs of Accounting or Plant Changes Resulting from AEC Ownership: APCO also requested that if, solely because of a sale of an ownership interest to AEC, APCO is required to incur additional costs, the incremental cost experienced should be for AEC's account. Examples of such costs would include costs of installing additional computer equipment to maintain books and records in a way different from the way APCO currently is accounting for costs, or costs to put additional equipment in the plant which costs arose solely because of an REA requirement relating to the environment which would not have otherwise been imposed on APCO as a result of the regulation of other governmental agencies. AEC has taken the position that these potential cost increases resulting solely from its acquisition of an ownership interest should be borne jointly by the parties in proportion to their interest. APCO continues to feel that it is unfair for it and its customers to be required to pick up any additional costs which arise solely to accommodate an ownership interest to AEC.

9. Liability to AEC: APCO has indicated its unwillingness to accept responsibility to AEC for the plant which AEC purchases regardless of the cause of any damage to AEC. We understand from AEC's willingness to purchase the plant "as is" that it has no objection to waiving claims for damages which it might claim as a result of the condition of the plant. There should be no ambiguity that if damage occurs to property in which AEC has joint ownership interest, AEC shall have no claim against APCO for damages it suffers under any theory including but not limited to contract, tort (including strict liability and misrepresentation) or laws of real property. Rather such costs resulting from such damage shall be borne pro rata between the joint owners on the basis of their ownership interests.

10. Indemnification against Third Party Claims: APCO requested that AEC also indemnify APCO against claims of AEC's wholesale purchasers or their customers for matters dealt with in the "as is" clause of the contract. AEC initially rejected this approach; however, it is presently reviewing the indemnification concept embodied in APCO's proposed Liabilities of the Parties clause and characterizes the proposal as "getting close". That clause would protect each owner against claims by the other owner's customers arising from plant outages and other problems.

11. Liability to Third Parties: APCO has requested recognition by AEC of its pro rata responsibility for liability to third parties (other than claims by customers of the other joint owner dealt with in 10 above). AEC's response has been that if APCO incurs any liability to any third party in the performance of its duties of plant operation, the amount paid by APCO will be considered an operating cost and apportioned between the parties. We take that to be an affirmative response which covers not just liability arising from performance of duties in operating the plant but also liability from defects in plant sold.

12. Waiver of Right of Partition: APCO has requested AEC waive not only its right as a joint owner seeking partition of the joinly owned property or sale for division, but also waive other common law incidents of joint ownership. The rights which AEC will have as to the properties will be set forth in the agreement. AEC has agreed to waive its right of partition, but wishes to explore waiver of other rights. There is a broad range of rights of joint owners which appear particularly inappropriate to force upon competitors. For instance, the common law right to participation in profits from the jointly held property would be repugnant to the forced arrangement currently being negotiated. The right of a joint owner to make use of property which does not interfere with use of such property by the other owner also is objectionable. These common law rights of joint owners are not appropriate in the context of the present relationship. Rather, the parties should concentrate on assuring that AEC has the appropriate rights necessary for it to enjoy the output of the Farley Plant resulting from its purchase and not spend endless hours assuring elimination of the rights of joint owners which are intended to apply only where the parties are engaged in a partnership effort to their mutual profit.

We are also concerned in connection with this and other areas of the proposed agreements with the potential

for AEC to argue later that agreements entered into are void for public policy reasons. For example, notwithstanding AEC's present willingness to waive its right of partition, we feel vulnerable to a later assertion that such restraint on alienation of property is unenforceable because of public policy in Alabama. This concern leads us to the conclusion that some mechanism must be included in the agreements to preclude such later assertions of unenforceability. We are exploring, for instance, the inclusion of a provision which permits termination of the agreement if either party seeks to have a court hold any provision of the agreement to be unenforceable. The unique, forced arrangement which has been ordered must be structured in a way in which the parties rights are clearly stated and the performance of the obligations are not frustrated by WPPSS type declarations of unenforceability.

13. Waiver of Right of Eminent Domain: AEC has requested that a provision be included so that the parties waive any right of eminent domain with respect to the other's interest in the Farley Plant. APCO does not object to such a provision but, by such waiver, does not wish to be understood as admitting that such a right actually exists.

14. Sale of Interest in Plant by AEC: APCO has requested, and AEC has agreed, that if AEC desires to transfer its interest in the plant to a third party, other than a transfer pursuant to mortgage or other financing arrangement, APCO shall have a right to purchase the plant at a price to be determined pursuant to a formula set forth in the agreement for sale of plant. AEC does not desire to agree on methodology for resale of the plant until the initial price for its purchase of the plant has been established. AEC has also stated it would not want a mortgage, lease back, merger, acquisition, etc. to be considered a sale. The clarification of this provision hopefully would not present a problem.

15. Incremental Taxes: APCO has requested, and AEC has indicated disagreement with, provisions for payment by AEC of any increased tax costs which APCO experiences and which result solely from entering into the joint ownership arrangement. If any such tax liability arises, it would be unconscionable for APCO to be forced to bear such costs. APCO continues to insist on this provision and AEC continues to refuse. In addition to its refusal to consider impacts of future taxes, AEC has indicated its unwillingness to pay for any income tax liability of APCO resulting from the sale to the extent such liability is offset by tax credits from

other portions of APCO's business. APCO requests that AEC reevaluate this position since the parties are in basic disagreement.

B. OPERATING AGREEMENT

1. APCO's Right to Determine Plant Operations and Maintenance: APCO has requested that it be given absolute authority, as agent for AEC, to make all determinations as to the operation of the plant. It has further requested AEC to commit to pay its pro rata share of costs of operation, capital improvements, acquisition of nuclear fuel, etc. Under the operating agreement which APCO would propose, AEC would agree to be bound by any agreement APCO enters into on behalf of the construction, operation and maintenance of the plant. Finally, APCO has requested AEC to waive any claims of any type which it might assert against APCO arising out of exercise of these operations.

APCO's basic position is that the plant was built by APCO to provide electric service to its customers in Alabama which it has a duty to serve. APCO has built and developed what it considers to be an extremely capable team to operate and manage the plant. It has not sought AEC's participation in the plant management and has expressed concern that such participation could not only be disruptive, it could be dangerous. AEC has agreed that it is not seeking direct participation in plant management, and that decisions relating to when the plant will be run, whether capital improvements are needed, and all other operational decisions of any nature, shall be vested solely in APCO. AEC has requested (and APCO has agreed) that it be informed in a timely fashion of major decisions, particularly those which affect AEC's budgeting process. AEC has also asked that APCO commit to make "no adverse distinction" in plant operation because of its ownership interest. APCO has agreed in a revised contract clause earlier sent to AEC.

The second issue is the right of AEC, after-the-fact, to question the decision made by APCO's employees in the operations of the plant. APCO has agreed that it will not operate the plant different from the manner it would otherwise have operated because of AEC's ownership position. AEC has asked, in addition, that APCO's operation of the plant be tested, after-the-fact, using a standard of conformity to "good utility practice". APCO views this standard as inherently inequitable given the circumstances of AEC's participation in the Farley Nuclear Plant. APCO rejects this "good utility practice" provision. Under the

scintilla rule in Alabama, AEC would most likely be able to present a jury question as to whether APCO exercised "good utility practice" in almost every case. Thus, in a situation similar to the incident which occurred at Unit 2 of the Three Mile Island Nuclear Plant, AEC could argue that there was a failure by APCO to use "good utility practice" and APCO must bear the cost, not only of its share of the clean-up, but also AEC's pro rata share as well. Were that to be permitted, APCO would be placed in the inequitable situation of having less than 100% ownership interest in the plant, and the right to enjoy less than 100% of the output of the plant, but would be forced to bear 100% of the risk of operation of the plant. APCO understands that AEC has expressed an understanding of the Company's problems with this clause.

A related issue involves the rights of AEC to recover from APCO for damages resulting from operations of the plant whether the damages are characterized as resulting from negligence, wantonness, or willfulness on the part of APCO employees. APCO has asked AEC to waive its right to seek damages against APCO for damages to or destruction of its interest in the plant facilities as a consequence of plant operations - regardless of the asserted basis for such damage. Thus, AEC would be precluded from seeking to have APCO pay for AEC's share of the cost even though AEC might assert that such damage resulted from a negligent, grossly negligent, wanton, reckless, or even willful act of APCO or one of its employees, agents or contractors.

This approach could be undermined, however, if AEC were to assert that such a waiver, even though agreed to, is void as against public policy. Some courts have held that contracts entered into at arms length in which one contracting party shifts the entire responsibility for his willful or wanton misconduct to the other contracting party are void as against public policy. The rationale for this rule is the judiciary's desire to avoid creating an attitude on the part of the indemnitee that he is not going to be held accountable for his actions. Here, since APCO has liability for in excess of 90 per cent of the consequences of its plant operations, the judicial concern that the contract would absolve APCO of responsibility for its conduct does not apply. Moreover, the risk sharing arrangement involved in the present transaction will be entered into pursuant to the NRC mandate that all costs be apportioned according to the parties' respective ownership shares.

APCO is convinced that the provision is not contrary to public policy in light of the foregoing, and seeks AEC's concurrence in that conviction. Even if such concurrence is forthcoming, however, because the courts have not directly spoken to an arrangement of this nature, more protection is needed to assure the costs associated with operating the plant are shared by the parties in proportion to the benefits they enjoy.

The second mechanism for avoiding the inequitable result, which was suggested by Mr. Rogers in our last meeting, is to place a cap on the amount of liability which would be owed by APCO to AEC under any theory of liability. APCO feels such a provision, similar to those which Westinghouse and General Electric include in all of their contracts for sale of electric equipment, should be included. We would agree that this type of clause, together with a clause of the type discussed in Paragraph 5 below, would be helpful in permitting the parties to close the gap in negotiations.

The third mechanism, a variation on the second, would be to predetermine the sole and exclusive remedy for any action on the part of APCO in operating the plant in a manner which a court later finds to be grossly negligent, wanton, reckless or willful.

Finally, as noted earlier in this letter, we are exploring additional means of assuring that provisions of the contract are enforced in accordance with the stated agreements of the parties. We would appreciate AEC's comments on these matters and its advice as to how the desired result can be achieved.

2. Payment of Pro Rata Share of Operating Costs: AEC has agreed on a "pay-as-you-go" basis, to share pro rata all costs associated with operation and maintenance of the plant, the making of capital improvements and additions, the acquisition of nuclear fuel, the costs of participation in nuclear industry organizations which are deemed desirable by APCO, and an appropriate allocation of APCO general corporate expense. AEC's caveats to this agreement are: (a) AEC does not want to make funds available for payment of such costs much in advance of APCO's payment of the cost; (b) AEC does not want to pay A&G expense if it is somehow covered in other rates or sales by the Company; and (c) AEC will accept and be bound by contracts which APCO enters on behalf of the plant operations but wants to be a partial assignee of such contracts. Caveat (a) and (c) should

present no insurmountable problems. Caveat (b) must be explored in greater depth with AEC to assure we are not caught in the regulatory lag trap that would suggest that since 100% of A&G has been allocated in rate cases to retail, wholesale or off-system sales customers, AEC has no responsibility for A&G expenses.

3. Operating Fees: APCO has proposed that it be paid a reasonable operating fee for running the plant on behalf of AEC. AEC has stated it feels that APCO should work for AEC for nothing. APCO has indicated its willingness to negotiate the level of the fees; however, AEC has steadfastly refused to recognize any responsibility to pay more than out-of-pocket expenses for services performed.

4. Incremental Costs Resulting Solely from AEC's Ownership Interest: APCO has requested provisions in the operating agreement under which AEC would be responsible for any incremental cost of operations which result solely from AEC having purchased an ownership interest in the plant. AEC has stated that all costs of operations should be viewed as project costs even though they would not have been incurred had AEC not had an ownership position.

5. Exclusion of Liability for Consequential Damages: AEC has agreed that a provision may be inserted in the agreement which would exclude liability for any consequential, special, incidental or indirect damages. This, as noted in Paragraph 1 above, may form part of the solution for the problems discussed there.

6. Decommissioning Cost and Cost of Disposal of Nuclear Fuel: AEC stated its willingness to pay its pro rata share of decommissioning and spent fuel disposal costs so long as their responsibility was recognized from the date of closing. APCO has agreed to AEC's criterion by adjusting the sales price to give AEC a pro rata credit for the decommissioning funds collected prior to the closing date, with AEC having responsibility for a pro rata share of total decommissioning costs. The arrangement for pro rata sharing of spent fuel disposal costs originally proposed by APCO, along with current legislation, will result in AEC paying disposal costs only for that portion of the fuel used to generate AEC's energy output for Plant Farley.

7. Fines and Penalties: AEC has also agreed that it would be responsible for its pro rata portion of any fines and penalties which arise out of plant operation where the imposition arises after the acquisition by AEC of an

ownership interest based on assertions made after such date. APCO will accept AEC's conditions; however, this too is an area which must be discussed further in light of a potential claim by AEC after the contract has been executed that the provision is void because it is contrary to "public policy". It must also be recognized that members of AEC being served by APCO prior to the acquisition and by AEC after the acquisition would be responsible for their pro rata portion of any fines and penalties regardless of the timing of assertions.

8. Term of Operating Agreement: The parties are in agreement that the operating agreement shall continue in effect until (1) all decommissioning associated with the plant has been completed; (2) all liability for waste produced or created by the plant has terminated, and (3) the plant site has been returned to a condition acceptable to APCO after decommissioning.

9. Insurance Coverage - Responsibility for Future Unquantifiable Expenses and Contingent Liabilities Not Covered by Insurance: The parties are in agreement on division of cost of the standard insurance coverages that shall be provided. APCO has requested that mechanisms be developed to assure AEC can come up with its pro rata share of self insurance under public liability insurance policies and Price Anderson Act requirements; retrospective premium adjustments, deductibles, and excess over limits under property insurance policies; as well as source of funds for contingencies not covered by insurance and future decommissioning costs, the amount of which is difficult to ascertain. AEC said it would explore development of such protection, but later withdrew its willingness to do so. In our latest meeting, AEC agreed to pursue, objectively, seeking REA's guarantee of the future unquantifiable expenses and contingent liabilities. Such a guarantee would relieve APCO's concern that AEC's lack of any equity in its business exposes APCO to the risk and costs associated with the contingent liabilities and presently unquantifiable expenses.

10. Defaults: AEC has suggested that defaults under the operating agreement be categorized as (1) failure of AEC to pay amounts owed when due, and (2) breaches of other obligations under the agreement. We have no problem with such categorization but would add one additional category, i.e., situations in which no actual breach has yet occurred but is imminent, such as bankruptcy petitions being filed or insolvency proceedings being initiated. The more important issue revolves around the remedy for breach. In the case of a

failure to pay money owed when due, AEC has suggested that default would not exist until the payment was at least 15 days late. APCO cannot accept that principle. The default exists if the payment is not made on time. The remedy for the default may involve a negotiated grace period within which AEC could cure the default by payment of the money due, plus interest and any additional costs incurred by APCO as a result of the default. It must be recognized that in some circumstances, where plant operation is jeopardized because of default on AEC's part to produce the money due, APCO and its customers can be severely damaged. This exposure may be relieved by AEC's maintenance of revolving funds which are available for draw by APCO, and recognition that failure to maintain such reserves would itself constitute default.

Notwithstanding our agreement as to categorization of defaults, we would note the need for a provision similar to that specified in Paragraph B.3(a)(10) of APCO's April 29, 1983 letter. As has been indicated earlier, we feel there should be a provision which permits the other party to terminate the arrangement if either party seeks to avoid obligations stated in the agreement on grounds of unenforceability of the agreement.

There does not appear to be any dispute about the range of remedies available in the event of default, only whether particular remedies listed should be available for less serious contract breaches by AEC. We are willing to explore these distinctions with AEC.

11. Budgeting and Cost Accounting Information: APCO has agreed to provide budgets and cost projections as well as cost accounting and financial and operating statistics which APCO generates in the course of its operations and planning for the Farley Plant.

12. Ad Valorem Tax Clause: APCO will accept the concept in the tax clause suggested by AEC under which AEC would assess its ownership interest in the Farley Plant separately for ad valorem tax purposes and for the purpose of any other taxes payable directly on the plant itself. APCO continues to insist on its position with respect to potential tax increases associated with sale of the interest in the plant to AEC and the income tax impact of such sale on APCO.

13. Audits of Cost: APCO agrees that language should be developed giving AEC appropriate audit rights, at its expense, to examine costs it is obligated to pay.

14. Regulatory Approval - Affirmative Obligation to Cooperate: APCO is willing to assure AEC that it will furnish AEC any information which APCO has that is needed for AEC to process any application for necessary approvals. APCO is unwilling to commit that it will forego any right or duty that it may have to object to the approval. It will make any formal application to NRC that may be required for NRC to determine whether AEC should become a licensee; however, in so doing it shall not waive its right to comment as it sees fit during the approval process.

15. Notice of Outages and Maintenance Periods: APCO agrees that it will notify AEC of planned maintenance and refueling outages in advance. APCO has also agreed that it will provide a signal to AEC, at AEC's expense, to permit AEC to monitor the output of the Farley Plant on an hourly basis.

16. AEC Access to Plant Farley: APCO has agreed that it would provide AEC reasonable rights to visit the plant provided such visits would not interfere in APCO's operations of the plant. AEC, in response, has stated it wished the right to station personnel at the plant full time, including provision of office space, to permit it to monitor plant operations. APCO objects to this request since, inter alia, such personnel are bound to try to justify their continued employment in such role by initiating continual inquiries of plant personnel as to what is going on. Such involvement in plant operations would only serve to direct the attention of plant personnel away from operating the plant.

17. REA Required Social Clauses: AEC has submitted several "social clauses" which are represented to be required by REA before it will loan money to AEC to finance purchase of an interest in the plant. We address each of these separately:

(a) Equal Opportunity Clause: APCO has, in its contract to supply electricity to federal buildings, an obligation in almost identical language to the obligations which would be imposed under the clause and APCO fully intends to perform such obligation. Paragraph (6) of the clause appears to permit AEC the right to terminate or cancel or suspend performance of the agreement if APCO is in

non-compliance with the Equal Opportunity Clause. Non-compliance with the clause by APCO should not permit AEC to avoid its obligations as joint owner under the operating agreement. Although we have reservations about including any clause that could affect the status of the agreement because of any incident of this character, if this clause must be inserted in the operating agreement, it must be made clear that any termination, cancellation or suspension of the contract pursuant to that clause shall not relieve AEC of its obligations to make payments for obligations incurred to that point in time and for future costs, such as decommissioning costs, which are attributable to AEC's period of ownership which arise after that point in time. Moreover, provision must be made for transfer by AEC to APCO of AEC's ownership interest in the plant should such provision for termination, cancellation or suspension of the contract be exercised by AEC.

(b) Non-Segregated Facilities Clause: The REA clause suggested by AEC is virtually identical to that of the clause APCO has entered with GSA. As such, we have no objection to the concept. We note that APCO's "breach" of this clause could also result in termination, cancellation or suspension of the operating agreement. Thus, we have the same reservations about this clause affecting the status of the agreement and the same post-termination provisions must be included as set forth above.

(c) Kickbacks Clause: APCO is not in a position to assure that it is familiar with all applicable statutes, rules and regulations relating to the "kickback" statute. Please furnish us a list of all statutes and a copy of all regulations which are relevant.

(d) Public Officials Not to Benefit Clause: We would like to explore with AEC and REA the obligations and limitations which would be created by this clause with respect to operations of the plant.

(e) Flood Insurance Act: APCO has no objection to this clause as long as it is recognized that if AEC does not pay for a portion of the plant facilities (such as the river intake structure which is partially submerged) because of the operation of this clause, AEC shall not be entitled to any of the output of the plant. Moreover, to the extent APCO becomes obligated through such clause to purchase flood insurance coverage that it would not otherwise have procured, such costs shall be for AEC's account.

(f) Historic Places Clause: Again, subject to the same conditions set forth in (e) above, APCO does not object to the inclusion of this clause in the operating agreement.

(g) Safety Clause: We object to inclusion of this clause since it could be interpreted as establishing a contractual obligation to AEC which is even more stringent than the "good utility practice" clause which has been discussed earlier.

(h) Buy American Clause: APCO will agree to negotiate the inclusion of this clause with AEC and REA but only with the condition that AEC shall be responsible for the incremental costs which result from the operation of the clause if, because of the clause, higher costs were experienced in plant operations.

(i) Environment Clause: APCO will agree to include a clause of this type in the operating agreement if it is made clear that AEC is responsible for incremental costs to APCO resulting from its operations. We would note that APCO has no present obligation to operate the plant in accordance with the Environmental Impact Statement prepared by NRC under NEPA. Rather, it is obligated to operate in accordance with its operating licenses.

C. OTHER AGREEMENTS

1. Sale of Short Term and Long Term Power: AEC has indicated its desire to discuss, as an integral part of the negotiations for purchase of an interest in the Farley Plant, the purchase of other bulk power from APCO. APCO has an existing contract with AEC to provide short term power, at a rate identified in the agreement. APCO has provided AEC voluntarily with a wheeling rate under which it may import power from third parties over APCO's lines. AEC is also interconnected with others at the Walter F. George Bus and is currently building an interconnection with SMEPA. APCO has also indicated to AEC its willingness to sell long term power to AEC on a basis similar to those which it is offering to other utilities. AEC has not been specific as to what it wants. In any event, APCO does not see this as a matter which should become enmeshed in the current negotiations.

2. Wheeling Agreement: AEC is to identify any needed changes which it feels must be made to the current agreements for provision of wheeling to AEC's off-system

wholesale customers in order to accommodate the purchase of a joint ownership interest in the Farley Plant.

3. Termination of Wholesale Power Agreements: APCO, at AEC's request, has agreed to waive the two year notice provision under the wholesale power supply agreements which APCO has with certain retail distribution cooperatives so that AEC can implement its 40 year all requirements contracts with those customers. The conditions for such waiver are: (a) APCO and AEC reach negotiated agreement for the sale of a percentage ownership interest; (b) the total load terminated without proper notice does not exceed AEC's negotiated share of the plant divided by 1.2; (c) AEC utilizes the Farley Plant power in serving such load lost by APCO; and (d) such waiver shall not be construed as a waiver of the notice provision in the future. In our last meeting, Mr. Rogers indicated that REA, as part of the procedure in determining whether a loan should be guaranteed by REA, will be inquiring whether power is available from any alternative sources. You should be aware, of course, that APCO stands ready and willing to continue to provide the same wholesale service to the distribution cooperatives which it is now serving at rates and under terms and conditions regulated by the Federal Energy Regulatory Commission.

We feel the above accurately sets forth the status of the parties' positions raised during negotiations to date. It should be recognized that other matters not covered in the parties' discussions to date are likely to be raised in future negotiations. We would invite your comments on these matters and your suggestions as to the next step in our negotiations. In that connection, Mr. Parish has written to request that a meeting be set up to discuss the income tax calculations reflected in APCO's initial offer as well as other cost matters. We shall do so and shall be in touch shortly with suggested times for such a meeting.

Sincerely,

Jesse S. Vogtle

Jesse S. Vogtle

Enclosures

cc: Mr. D. Biard MacGuineas
Mr. Jeff Parish

"AS IS" SALE WITHOUT WARRANTY: THE FACILITIES TO BE SOLD UNDER THIS AGREEMENT SHALL BE SOLD ON AN "AS IS - WHERE IS" BASIS. APCO MAKES NO WARRANTY OR REPRESENTATION WHATSOEVER, EXPRESS, IMPLIED OR STATUTORY, AND DISCLAIMS ANY AND ALL WARRANTIES, INCLUDING, WITHOUT LIMITATION, ANY REPRESENTATION OR WARRANTY AS TO THE VALUE, QUANTITY, QUALITY, CONDITION, SALABILITY, OBSOLESCENCE, MERCHANTABILITY, FITNESS OR SUITABILITY FOR USE OR WORKING ORDER OF ALL OR ANY PART OF SAID FACILITIES. NOTWITHSTANDING THE FOREGOING, AEC SHALL HAVE THE BENEFIT, IN PROPORTION TO AEC'S PERCENTAGE OWNERSHIP INTEREST, OF ALL MANUFACTURERS', VENDORS' AND CONTRACTORS' WARRANTIES AND ALL PATENTS AND LICENSES, IF ANY, RUNNING TO APCO IN CONNECTION WITH THE FACILITIES TO BE SOLD UNDER THIS AGREEMENT, SUBJECT TO THE PROVISIONS OF SECTION ____ HEREOF DEALING WITH CONTRACTS WITH THIRD PARTIES.

CONTRACTS WITH THIRD PARTIES

1. Acceptance of Contract Provisions: AEC recognizes that APCO has entered into contracts with numerous parties in connection with the construction, operation and maintenance of the facilities covered by this agreement and in such contracts has agreed to certain matters including, but not limited to, limitations on the liability of such contractors for work performed or materials furnished, restrictions on warranties, agreements to indemnify the contractors from liability and other provisions. AEC agrees to accept and be bound by the provisions of all such agreements and further agrees that it waives any claims against APCO for having entered into such contracts or agreed to the provisions thereof. AEC also recognizes that a number of the APCO contracts relating to the facilities contain provisions that require APCO to obtain from any assignee or transferee prior to any assignment of rights under such contract or any transfer of materials, equipment or work product, or any interest therein obtained by APCO pursuant to such a contract, an agreement by such assignee or transferee that it will be bound by all of the requirements for financial protection, waivers, releases, indemnifications, limitations of liability and further transfers or assignments that bind APCO under such contracts. AEC agrees that it will be so bound by the requirements for financial protection, waivers,

releases, indemnification, limitation of liability and further transfers that bind APCO as they now exist or may in the future be with respect to all contracts relating to the facilities.

2. Enforcement of Rights Under Contracts: AEC covenants that, without the written consent of APCO, it will not threaten suit or bring suit against third parties or otherwise make any claim under any contract or arrangement relating to the facilities and AEC recognizes that APCO has complete and exclusive authority, under the agreements, with respect to all such matters. If AEC desires for suit to be threatened or brought or otherwise for any claim to be made, or desires that such action contemplated by APCO shall not be taken, AEC shall, by written notice to APCO, request APCO so to act or refrain from acting. Upon receipt of such notice the parties shall arrange for consultation on the questions raised within 10 working days thereafter, or such lesser period of time as APCO, in its sole discretion, shall specify in the light of circumstances requiring a more expeditious determination. APCO shall not make its determination until after such consultation but such determination by APCO shall be final and binding on AEC.

ATTACHMENT 10

PURCHASE AND OWNERSHIP AGREEMENT FOR JOINT OWNERSHIP INTEREST IN THE JOSEPH M. FARLEY NUCLEAR PLANT UNITS ONE AND TWO BETWEEN ALABAMA POWER COMPANY AND ALABAMA ELECTRIC COOPERATIVE, INC.

PURCHASE AND OWNERSHIP AGREEMENT
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ATTACHMENT 8

PURCHASE AND OWNERSHIP AGREEMENT FOR JOINT OWNERSHIP INTEREST IN THE JOSEPH M. FARLEY NUCLEAR PLANT UNITS ONE AND TWO BETWEEN ALABAMA POWER COMPANY AND ALABAMA ELECTRIC COOPERATIVE, INC.

THIS AGREEMENT is made and entered into as of the _____ day of _____ 1984, by and between Alabama Power Company (APCO), an Alabama corporation with its principal office at 600 North 18th Street, Birmingham, Alabama, and ALABAMA ELECTRIC COOPERATIVE, INC. (AEC), an electric cooperative organized under Alabama law with its principal office at _____ _____, Andalusia, Alabama:

WITNESSETH

WHEREAS APCO is an electric utility organized and existing under the laws of the State of Alabama; and

WHEREAS APCO has constructed and operates a nuclear plant near Dothan, Alabama, referred to as the Joseph M. Farley Nuclear Plant, Units 1 and 2, (the "Farley Nuclear Plant") subject to the requirements of the licenses issued by the Nuclear Regulatory Commission; and

WHEREAS AEC is a generation and transmission cooperative organized and existing under the laws of the State of Alabama; and

WHEREAS, on August 10, 1981, the Nuclear Regulatory Commission amended APCO's license for the Farley Nuclear Plant by requiring APCO to offer to sell to AEC an undivided ownership interest in the Farley Nuclear Plant; and

WHEREAS, in accordance with the foregoing, APCO has offered to sell to AEC, on the terms and conditions set forth herein, a 6.26 percent undivided ownership interest in the Farley Nuclear Plant; and

WHEREAS, the parties recognize that the transactions contemplated hereby were solely the product of administrative and judicial decrees designed to satisfy certain antitrust concerns by providing AEC with access to power generated by the Farley Nuclear Plant, and that such decrees were not intended to provide AEC with other incidents of joint ownership not explicitly granted herein which might otherwise accompany the sale of such an ownership interest; and

WHEREAS, AEC has agreed to the purchase from APCO on the terms and conditions set forth here, a 6.26 percent undivided ownership interest in the Farley Nuclear Plant.

WHEREAS, the parties agree that the undertakings contemplated by the Basic Agreements satisfy the requirements of the August 10, 1981 license condition amendment.

NOW, THEREFORE, in consideration of the premises and mutual obligations hereinafter stated, the parties hereto agree as follows:

ARTICLE I

Definitions

1.01 Actual Cost of Funds During Construction. The Actual Cost of Funds During Construction shall be that amount equal to the average cost of money to APCO during the period during which funds were invested by APCO in the Facilities being constructed.

1.02 Agreement. This Agreement for the sale of an ownership interest in the Joseph M. Farley Nuclear Plant Units 1 and 2 dated as of _____ between APCO and AEC.

1.03 Affiliates. Any corporation or other entity which controls, is controlled by, or is under common control with any party to this Agreement.

1.04 Basic Agreements. This Agreement, the Operating Agreement, and the Nuclear Fuel Agreement.

1.05 Capacity. The capability of producing energy, measured in megawatts.

1.06 Capability. The net summer or winter (as applicable) rating of Farley Unit 1 or Farley Unit 2, measured in megawatts, as determined by APCO.

1.07 Common Facilities. All those facilities, exclusive of Farley Unit 1, Farley Unit 2, Nuclear Fuel and Operating Inventory, which are purchased, leased or otherwise obtained only in connection with the construction, operation and maintenance of more than one nuclear unit located at the Joseph M. Farley Nuclear Plant. Common Facilities are more specifically described as of the date hereof in Exhibit "A".

1.08 Facilities. Farley Unit 1, Farley Unit 2, the Common Facilities and the Operating Inventory, but excluding Nuclear Fuel, which is the subject of the Nuclear Fuel Agreement.

1.09 Farley Plant. The nuclear generating plant located in Houston County, Alabama, which, for the purpose of this Agreement shall mean Farley Unit 1, Farley Unit 2, the Common Facilities and the Operating Inventory but excluding Nuclear Fuel which is the subject of the Nuclear Fuel Agreement. It is interded that this term be identical in meaning with the term "Facilities."

1.10 Farley Unit 1. The nuclear generating unit located in Houston County, Alabama, and designated as Farley Unit 1 (more specifically described in Exhibit "B" hereto), including the

surface interest in the land on which such unit is located, but excluding the Common Facilities, the Nuclear Fuel, the Operating Inventory, and Farley Unit 2.

1.11 Farley Unit 2. The nuclear generating unit located in Houston County, Alabama, and designated as Farley Unit 2 (more specifically described in Exhibit "C" hereto), including the surface interest in the land on which such unit is located, but excluding the Common Facilities, the Nuclear Fuel, the Operating Inventory, and Farley Unit 1.

1.12 Immediately Available Funds. Funds which are good and available to the payee on the date when paid.

1.13 Indenture. The Indenture dated as of January 1, 1942, from APCO to Chemical Bank, as trustee, as supplemented from time to time.

1.14 Interest Rates.

(a) The Special Interest Rate. A rate per annum equal to the prime rate of AmSouth Bank, N.A., Birmingham, Alabama, or its successor, in effect from time to time plus three percentage points (3%).

(b) The Regular Interest Rate. An interest rate per annum equal to the actual weighted cost of APCO's short term financing for the period in question or, if APCO has no short term financing outstanding at the time, the prime rate of

AmSouth Bank, N.A. as in effect from time to time. Short-term financing shall be all debt financing other than long term debt as defined by the Uniform System of Accounts.

1.15 Lien. Any encumbrance, lien, charge or security interest upon or in any of the facilities.

1.16 Members of AEC. For the purpose of this agreement those presently existing or future rural electric distribution cooperatives and municipal corporations and utility boards, and others which are members of AEC, their successors and assigns. For the purposes of this agreement, the presently existing AEC members shall mean those cooperatives, municipal entities and corporations, together with their respective delivery points, listed in Exhibit "D".

1.17 New Investment. The net book cost to APCO for all additions, improvements, betterments and replacements related to the Facilities incurred after the closing date, accounted for by APCO as utility plant under the uniform system of accounts. New investments shall not include Actual Cost of Funds During Construction in the case where AEC is paying its proportionate share of New Investment in accordance with the provisions of the Operating Agreement but shall include such Actual Cost of Funds in the case where APCO has previously incurred such a cost.

1.18 NRC. The Nuclear Regulatory Commission including any successor governmental agency having jurisdiction over the operation of the Farley Plant.

1.19 Nuclear Fuel. For the purpose of this agreement, nuclear fuel shall have the meaning defined in the Nuclear Fuel Agreement.

1.20 Nuclear Fuel Agreement. The Nuclear Fuel Agreement between APCO and AEC of even date herewith.

1.21 Operating Agreement. The Operating Agreement between APCO and AEC of even date herewith.

1.22 Operating Inventory. Equipment, spare parts (including spare parts in which APCO may have an interest because of an agreement for pooling of inventory with others), tools, goods and supplies (excluding Nuclear Fuel) which may be used for the operation, maintenance, modification of the Facilities and recorded on APCO's books of account in accordance with the Uniform System of Accounts.

1.23 Percentage Ownership Interest of AEC. Except as otherwise modified by the operation of the provisions of Articles XV and XVI hereof, an undivided ownership interest in the Facilities equal to 6.26% in each of Farley Unit 1, Farley Unit 2, the Common Facilities and the Operating Inventory.

1.24 Percentage Ownership Interest of APCO. Except as otherwise modified by the operation of the provisions of Articles XV and XVI hereof, an ownership interest equal to 93.74% in each of Farley Unit 1, Farley Unit 2, the Common Facilities and the Operating Inventory.

1.25 REA. The Rural Electrification Administration.

ARTICLE II

Purchase of AEC's Percentage Ownership Interest

2.01 Purchase of AEC's Percentage Ownership Interest in the Facilities at Closing. At Closing, subject to the terms and conditions set forth herein, APCO shall sell and convey and AEC shall purchase and pay for AEC's percentage ownership interest in the facilities at the Closing Date.

2.02 Conveyances. At Closing, APCO shall consummate the transfer of the Percentage Ownership Interest of AEC by delivery of:

(a) A statutory warranty deed substantially in the form of Exhibit "E" hereto making APCO and AEC tenants in common but subject to the limitation on such tenancy in common as specified therein and in Section 2.03 hereof;

(b) An assignment agreement substantially in the form of Exhibit "F" hereto transferring an undivided ownership interest in APCO's rights and obligations under those certain contracts, licenses and permits listed in Exhibit "F" hereto for the purchase, repair, construction, ownership and operation of the Facilities;

(c) A bill of sale substantially in the form of Exhibit "G" hereto conveying an undivided ownership interest in all property listed thereon;

(d) Releases of such undivided ownership interests in the Facilities from the lien of the Indenture of Mortgage.

2.03 Limitation on AEC's Rights as Tenant in Common. The parties recognize that the sale of an ownership interest in the Farley Nuclear Plant to AEC is the product of administrative and judicial orders designed to satisfy antitrust concerns by providing AEC with an ownership interest in the Facilities and not because APCO and AEC mutually determined that it would be in their respective best interests to enter into the arrangement contemplated hereby. Accordingly, APCO and AEC agree that the normal incidents of tenancy in common shall not be applicable to the conveyance of AEC's Percentage Ownership Interest, and that AEC shall have no rights as

tenant in common other than those specifically enumerated in the Basic Agreements.

2.04 Entitlement to Available Capacity. (a) After closing, except as otherwise provided in this Agreement, AEC and APCO shall be entitled to the available capacity of Farley Units 1 and 2 as follows:

APCO:	93.74%
AEC:	6.26%

(b) With respect to Farley Units 1 and 2, AEC shall be entitled to AEC's Percentage Ownership Interest of the available capacity in each such unit. Available capacity is defined as that capacity of the particular unit that is available for operation as determined by APCO. Reductions in unit capacity arising from any cause, including but not limited to, operating limitations or regulatory requirements, during any hour in a billing period, shall result in proportional reduction in AEC's share of the available capacity.

2.05 Modification of Capacity Entitlement. Notwithstanding the foregoing sections of this Article II, the parties' entitlement to available capacity and associated energy may be modified from time to time in accordance with the operation of Articles XV and XVI hereof and the procedures set forth in Article ____ of the Operating Agreement.

2.06 Second Mortgage Lien. In consideration of APCO's obligations to AEC under the Basic Agreements, AEC agrees to grant to APCO, at the Closing, a second mortgage lien on all property of AEC, including the Facilities, to secure the payment by AEC of those amounts due APCO pursuant to this Agreement, the Operating Agreement and the Nuclear Fuel Agreement. Such second mortgage lien shall be evidenced by a second mortgage and deed of trust substantially in the form of Exhibit "H" hereto. As set forth in Exhibit "H", the parties agree (i) that any default in the payment of money under AEC's first mortgage shall (after the expiration of the grace period provided for in Exhibit "H") be a default under the second mortgage granted hereunder, and (ii) that upon any such default under AEC's first mortgage, APCO shall be given timely notice by AEC of the occurrence of such default and APCO shall have the right to cure such default.

2.07 Future Property Conveyances. If, in the future, additional facilities must be built so as to constitute part of Farley Unit 1 or Farley Unit 2 on land to which AEC does not have an ownership interest, APCO shall convey to AEC its Percentage Ownership Interest in the surface of such land for an amount equal to AEC's Percentage Ownership Interest times APCO's total book costs. Should APCO desire to construct facilities, or make other use of any real property conveyed to AEC under this Agreement which facilities or use is not related to the Farley Plant, and should such facilities or use

not interfere with the Farley Plant operations, then AEC shall reconvey its ownership interest in that real property, free of any lien or encumbrance, at AEC's original cost of such land prorated on a per acre basis over all land acquired by AEC at closing. After the Farley Plant has been decommissioned, as determined by APCO, AEC shall, at APCO's option, reconvey its ownership interest in the real property, free of any lien or encumbrance, at AEC's original cost of such land prorated on a per acre basis over all land acquired by AEC at closing. AEC further agrees, at APCO's option, to convey to APCO, free of any lien or encumbrance, all interest in real property which has theretofore been conveyed to it which constitutes part of the Farley Plant, in the event of any default by AEC, such conveyance to be made in accordance with and under the circumstances described in Articles XV and XVI hereof. AEC hereby appoints APCO its attorney-in-fact to execute on its behalf any deed, or other instrument, in order to consummate any such conveyance.

ARTICLE III

Payments for AEC's Percentage Ownership Interest

3.01 Payment. (a) The purchase price of the Facilities shall be in the amount of _____ Dollars ($_____), which is allocated among the various elements constituting the price as reflected in Exhibit "I". At the Closing, AEC shall pay to APCO the purchase price for

AEC's Percentage Ownership Interest as prescribed in Exhibit "I" hereto.

3.02 Payments for Retirements and Decommissioning Costs: Option to Purchase the Facilities. (a) APCO shall have the authority to determine when the any or all of the Facilities shall no longer be used or useful in the operation of the Farley Plant and when they shall be retired from service, with or without replacement. Cost of retirements and salvage credits from the sale or other uses, if any, shall be shared by the parties in proportion to their respective Percentage Ownership Interest; provided, however, APCO shall have a right to set-off any such salvage credits against any amount owed by AEC to APCO under the Basic Agreements or any other agreement between APCO and AEC.

(b) APCO shall retain such powers hereunder as shall be necessary for the disposition of all tangible and intangible property (excluding the land constituting a part of that facility) and shall dispose of such property as promptly as practicable. Upon such disposition, APCO shall distribute the proceeds thereof, if any, to AEC in accordance with its percentage ownership interest hereunder; provided, however, APCO shall have a right to set-off any such proceeds against any amount owed by AEC to APCO under the Basic Agreements or and other agreement between APCO and AEC.

(c) Upon the issuance of a lawful and enforceable order terminating the operation of any portion of the Facilities, from the Government of the United States or from the State or any of the departments, agencies, officials or courts thereof having jurisdiction, or upon a determination by APCO that the whole or any portion of the Facilities should be retired, the Parties shall bear all costs incurred for decommissioning in proportion to their respective Percentage Ownership Interests, as they may change from time to time (based on the principles governing such changes as reflected in Section 11.03), for whatever period of time is necessary, whether pursuant to regulatory requirements or otherwise, and to provide for any restoration of the site deemed appropriate by APCO, to complete the decommissioning and retirement process so that, in APCO's sole judgment, no further expenditure of funds is required. As security for payment of its obligation ultimately to pay its share of such decommissioning costs, AEC shall at all times maintain the agreements provided for in Section 4.02(b) and 4.02(c) in addition to the security provided in Section 2.06 hereof. Decommissioning costs shall include, but not be limited to, any costs which must be provided for in advance of decommissioning, and any additional costs which are incurred during or after decommissioning, including monitoring of the site, whether such costs shall result from regulatory requirements or otherwise.

(d) After decommissioning when either unit, or any portion of the real property constituting a part of the Facilities is to be retired, APCO will furnish written notice of such retirement and decommissioning to AEC. APCO shall have the option, which may be exercised by the giving of thirty (30) days written notice to AEC, to purchase such real property from AEC at the original cost to AEC for the land.

(e) After the decision to decommission has been made, APCO shall proceed with the decommissioning unless the Parties agree to enter into a separate agreement to decommission the Facilities. Any such agreement shall contain no provision which is inconsistent with any term of this Agreement.

3.03 Payment for Other Costs. The Parties agree to pay those costs relating to their respective ownership interests that are not otherwise provided for herein if such costs are incurred in the planning, design, engineering, construction, procurement, making of new investment, modification, ownership (including payment of any ad valorem or other taxes), retirement or decommissioning of the Facilities. To the extent possible, each party shall separately report, file returns with respect to, and be responsible for and pay all ad valorem, franchise, business, or other taxes and fees, except payroll and sales and use taxes, arising out of each party's ownership of Farley Plant. However, to the extent that such taxes or fees may be levied on or assessed against the total plant, or

its operation, or on the parties in such a manner so as to make impossible the carrying out of the foregoing provisions, or upon mutual agreement of the parties, then such taxes or fees shall be shared pro rata based upon the respective ownership percentages of the parties. AEC shall pay (or reimburse APCO if APCO has incurred) incremental costs experienced by APCO solely as a result of the sale to AEC of an ownership interest in the Farley Plant including, but not limited to: (a) the adverse impact on APCO of any tax legislation, or interpretation of tax laws; (b) special accounting requirements; (c) requirements of REA, or other governmental agency, which APCO would not have incurred but for AEC's participation.

3.04 Methods of Payment. All payments required to be made by either Party under this Agreement in excess of $10,000 shall be paid on or before the payment date in immediately available funds by delivery (before 11:00 a.m., Birmingham time) of either a Federal Reserve check or evidence of bank wire to the other Party's account, at a bank designated by such Party. If any such payment is to be made by bank wire, the Party entitled to the payment shall advise the other Party of the appropriate bank and account number at least one business day before the payment is due. All other payments required to be made under this Agreement may be made by check deposited in the United States Mail three (3) days prior to the date due, first-class postage prepaid, and addressed to Treasurer,

Alabama Power Company, P. O. Box 2641, Birmingham, Alabama, 35291, if payable to APCO, and addressed to General Manager, Alabama Electric Cooperative, Inc., P. O. Box 550, Andalusia, Alabama, 36420, if payable to AEC unless a different addressee or address shall have been designated by either Party by notice in writing to the other Party.

ARTICLE IV

Representations and Warranties

4.01 Representations and Warranties of APCO. APCO represents and warrants as follows:

(a) APCO is a corporation duly incorporated and validly existing, in good standing, under the laws of Alabama.

(b) APCO has, or at the Closing will have, power to convey, by statutory warranty deed, title to AEC's Percentage Ownership Interest in the real estate and fixtures constituting the Facilities, free and clear of all liens, except for such exceptions as may exist in the titles acquired by APCO and Permitted Encumbrances.

4.02 Representations and Warranties of AEC. AEC represents and warrants as follows:

(a) AEC is a generation and transmission cooperative duly incorporated and validly existing, in good standing,

under the laws of Alabama; is duly qualified and authorized to do business; and is in good standing in each jurisdiction where the character of its properties or the nature of its actions makes such qualification necessary, and has the corporate power to carry on its business as now being conducted; and possesses all Federal and State authority and local franchises necessary for the maintenance and operation of its properties and business with such minor exceptions as will not materially interfere with the ownership and operation of the Facilities.

(b) Consummation of the transactions contemplated hereby and performance of the obligations imposed by the Basic Agreements by AEC will not result in violation of any laws, ordinances, or governmental rules to which it is subject. AEC either has obtained, or at the Closing Date shall have obtained, all necessary governmental approvals and consents (including the approval of REA) in connection with the consummation by AEC of the transactions hereby contemplated and the performance by it of the Basic Agreements and REA has entered into and will be bound by the Guaranty Agreement set forth in Exhibit "J" attached hereto.

(c) The consummation of the transactions hereby contemplated and the performance by AEC of the Basic Agreements will not result in the breach of, or constitute a default under,

the Articles of Incorporation or By-Laws of AEC or any indenture, mortgage, deed of trust, bank loan or credit agreement, or other agreement or instrument to which AEC is a party or by which AEC or its properties may be bound or affected, or result in the creation of any lien, charge, security interest or encumbrance upon any property of AEC (other than any lien, charge, security interest or encumbrance created by AEC as a result of its purchase of AEC's Percentage Ownership Interest at the Closing and other than Permitted Encumbrances), and AEC is not in default under any term of any such agreement or instrument.

(d) On the date hereof there exists, as to AEC, no Event of Default or event or condition which, with the giving of notice or the lapse of time or both, would constitute an Event of Default.

(e) Each of AEC's Members has entered into and will be bound by the Special Guaranty Agreement set forth in Exhibit "K" attached hereto on the Closing Date.

4.03 Survival. All representations and warranties made by the Parties in or under the Basic Agreements (and all representations and warranties contained in any certificate or other instrument delivered by any of the Parties pursuant to the Basic Agreements) shall survive the execution and delivery of the Basic Agreements and any action taken or documents delivered pursuant thereto.

ARTICLE V

The Closing and Closing Date

5.01 Time and Place. The Closing shall be held commencing at 10:00 a.m., Birmingham, Alabama time, on such date on or before December 31, 1984 as the Parties shall agree, at 600 North 18th Street, Birmingham, Alabama, provided that, pursuant to Article VI hereof, all conditions precedent to Closing have occurred, unless waived by the Party benefitted thereby. AEC hereby agrees to close promptly upon obtaining the financing that it has covenanted to obtain in accordance with Section 9.02 hereof. Since time is of the essence, the Closing shall not be later than December 31, 1984.

5.02 Termination of Liability. If the conditions specified in Article VI hereof shall not have been satisfied on or before December 31, 1984, all liability of the Parties under this Agreement shall terminate other than each Party's liabilities for its own expenses.

ARTICLE VI

Conditions to Closing

6.01 Conditions Precedent to APCO's Obligations. All obligations of APCO to AEC are subject to the fulfillment, on or prior to the Closing, of each of the following conditions:

(a) All instruments relating to the sale and purchase of AEC's Percentage Ownership Interest, and all proceedings taken on or prior to the Closing in connection with the performance of the Basic Agreements shall be satisfactory to APCO and APCO shall have received copies of all such documents or other evidence as it may reasonably request in order to establish the rightful consummation of such transactions and the taking of all necessary action in connection therewith, in form (as to certification and otherwise) and substance satisfactory to APCO.

(b) All representations and warranties of AEC in or under the Basic Agreements (and all representations and warranties contained in any certificate or other instrument delivered by AEC pursuant to the Basic Agreements) shall be true with the same effect as though such representations and warranties had been made on and as of such date (except as affected by transactions contemplated by the Basic Agreements) and AEC shall have performed all agreements on its part required by the Basic Agreements to be performed on or prior to such date; and APCO shall receive a certificate, dated such date, of the President and General Manager of AEC and by a nationally recognized independent accounting firm, to such effect.

(c) APCO shall have obtained all necessary releases and other required documents from the trustee under the Indenture

of Mortgage permitting the conveyances pursuant to Article II hereof, accompanied by an opinion of counsel of the trustee substantially to the effect that such trustee has the corporate power and authority to execute and deliver such releases and other documents and that such releases and other documents have been duly executed and delivered and constitute the legal, valid and binding obligations of such trustee enforceable against it in accordance with their terms.

(d) The following governmental and regulatory approvals required to be obtained prior to the Closing by APCO and AEC shall have been obtained and shall not have been modified (unless any such modification shall have been accepted in writing by the Parties) or rescinded, are in full force and effect and all appeal periods shall have expired, such approvals to be evidenced by the delivery to APCO and AEC of certification of the governmental approvals referred to in this Article:

The Alabama Public Service Commission

The Alabama Department of Finance

REA

NRC

and such approvals shall not contain any conditions unacceptable to APCO.

(e) APCO shall have received a written ruling from the Internal Revenue Service satisfactory in form and content to

APCO, to the effect that for Federal income tax purposes only (i) the arrangement created by the Basic Agreements will be treated as a partnership and not as an association taxable as a corporation and that APCO and AEC may elect to exclude such arrangement from the application of Subchapter K of the Internal Revenue Code of 1954, as amended, and (ii) as a result of the Basic Agreements APCO will not be denied the right to any investment tax credits, liberalized depreciation or other available tax benefits with respect to its ownership interest.

(f) AEC and each of AEC's Members shall have executed and delivered to APCO a release and covenant not to sue, substantially in the form of Exhibit "L" hereto, together with certified resolutions of the respective Boards of Directors authorizing such execution and delivery.

(g) APCO shall have received a satisfactory certificate or certificates, each signed by appropriate officers of AEC and dated as of the Closing Date, as to all questions of fact involved in the conditions set forth in this Section 6.01.

(h) APCO shall have received the Special Guaranty Agreements of AEC's Members and the Guaranty Agreement of REA.

(i) APCO shall have received opinions of counsel for AEC, dated the Closing Date, substantially in the forms of Exhibits "M" and "N" hereto.

(j) APCO shall have received a certified copy of resolutions duly adopted by the Board of Directors of AEC ratifying or approving all of the transactions contemplated by the Basic Agreements.

(k) AEC shall have made available in immediately available funds the purchase price required to be paid at the Closing, as required by Section 3.01.

(l) All actions required to be taken by REA to permit the consummation of this Agreement shall have been taken and APCO shall have received evidence, satisfactory to it, that a loan agreement between AEC and the REA or other lender(s) satisfactory to APCO has been duly executed and is a legal, valid and binding obligation of AEC, the REA or other lender(s) sufficient to finance AEC's Percentage Ownership Interest at the time of Closing, in the Facilities.

6.02 Conditions Precedent to AEC's Obligations. All obligations of AEC to APCO are subject to fulfillment, on or prior to the Closing, of each of the following conditions:

(a) All instruments relating to the sale and purchase of AEC's Percentage Ownership Interest and all proceedings taken on or prior to the Closing in connection with the performance of the Basic Agreements shall be satisfactory to AEC and AEC shall have received copies of all such documents.

(b) All representations and warranties by APCO in or under the Basic Agreements (and all representations and warranties contained in any certificate or other instrument delivered by APCO pursuant to the Basic Agreements) shall be true with the same effect as though such representations and warranties have been made on and as of such date (except as affected by transactions contemplated by the Basic Agreements), and APCO shall have performed all agreements on its part required by the Basic Agreements to be performed on or prior to such date; and AEC shall receive a certificate, dated such date, of an Executive Vice President and a principal financial or accounting officer of APCO to such effect.

(c) APCO shall have obtained all necessary releases and other required documents from the trustee under the Indenture permitting the conveyance pursuant to Article II hereof.

(d) The following governmental and regulatory approvals required to be obtained prior to the Closing by APCO and AEC shall have been obtained and shall not have been modified (unless any such modification shall have been accepted in writing by the Parties) or rescinded, are in full force and effect and all appeal periods shall have expired, such approvals to be evidenced by the delivery to APCO and AEC of certification of the governmental approvals referred to in this Article:

The Alabama Public Service Commission

The Alabama Department of Finance

REA

NRC

and such approvals shall not contain any conditions unacceptable to AEC.

(e) AEC shall have received a written opinion of its counsel, satisfactory in form and content to AEC to the effect that for Federal income tax purposes only (i) the arrangement created by the Basic Agreements will be treated as a partnership and not as an association taxable as a corporation and that AEC and APCO may elect to exclude such arrangement from the application of Subchapter K of the Internal Revenue Code of 1954, as amended, and (ii) as a result of the Basic Agreements (provided AEC otherwise qualifies for such tax benefits) AEC will not be denied the right to any investment tax credits, liberalized depreciation or other available tax benefits with respect to its ownership interest.

(f) AEC shall have received a satisfactory certificate or certificates, each signed by appropriate officers of APCO and dated the Closing Date, as to all questions of fact involved in the conditions set forth in this Section 6.02.

(g) The Special Guaranty Agreements of AEC's Members and the Guaranty Agreement of REA shall be in full force and effect.

(h) AEC shall have received an opinion of counsel for APCO, dated the Closing Date, substantially in the form of Exhibit S hereto.

(i) AEC shall have received a certified copy of resolutions duly adopted by the Board of Directors of APCO ratifying or approving all of the transactions contemplated by the Basic Agreements.

ARTICLE VII

Nuclear Fuel

7.01 Sale and Purchase of Nuclear Fuel. The sale by APCO and the purchase by AEC of Nuclear Fuel is provided for in the Nuclear Fuel Agreement and not by this Agreement, except to the extent that (a) provisions of this Agreement specifically refer to Nuclear Fuel or the Nuclear Fuel Agreement, or (b) provisions of this Agreement are incorporated by reference in the Nuclear Fuel Agreement.

ARTICLE VIII

Management of the Facilities; "As-Is" Sale; Liability and Allocation of Risk; and Contracts for the Facilities

8.01 APCO as Agent for AEC. (a) AEC hereby appoints APCO (such appointment shall be irrevocable, for the term of this

Agreement, and coupled with an interest) its sole agent subject only to AEC's right of reasonable inspection through authorized representatives at times agreeable to APCO, to act on its behalf for the planning, design, engineering, construction, procurement and making of New Investment, and the modification, operation, maintenance, retirement and decommissioning of the Facilities and authorizes APCO in the name of and on behalf of AEC to take all actions which, in the discretion and judgment of APCO, are deemed necessary or advisable to effect the planning, design, engineering, construction, procurement, making of New Investment, modification, operation, maintenance, retirement and decommissioning of the Facilities, including, without limitation, the following:

(i) The making of such agreements and modifications of existing agreements and the taking of such other action as APCO deems necessary or appropriate, in its sole discretion, or as may be required under the regulations or directives of such governmental bodies and regulatory agencies having jurisdiction, with respect to the construction, acquisition and completion of any additions, improvements, betterments and replacements related to the Facilities, or the procurement, replacement, modification or renewal of all or any part of the Farley Plant, and if necessary, the retirement, disposal, decommissioning or salvaging of any part thereof.

(ii) The execution and filing with such governmental bodies and regulatory agencies having jurisdiction of applications, amendments, reports and other documents and filings for or in connection with licensing and other regulatory matters with respect to Facilities; and

(iii) The receipt on AEC's behalf of any notice or other communication from any gcvernmental body or regulatory agency having jurisdiction, as to any licensing or other regulatory matter with respect to Facilities.

(iv) Subject to Section 8.03, the right to bring suit on behalf of AEC or AEC and APCO jointly for any cause of action arising out of or in connection with rights or obligations under the Basic Agreements.

(b) As relates to all third parties, this agency designation shall be binding on AEC and such appointment shall be deemed in effect by each third party until termination of this Agreement pursuant to the terms hereof and such third party receives written notification from APCO of any termination thereof.

(c) APCO accepts such appointment.

(d) AEC shall promptly take all necessary action to execute any agreements with respect to the Facilities as and when requested by APCO.

(e) AEC expressly agrees that APCO does not, by this Agreement, assume any risks or liabilities with respect to AEC's Percentage Ownership Interest and that the amounts paid and payable to APCO under the Basic Agreements are determined on the basis that APCO does not assume any such risks or liabilities.

8.02 "AS IS" SALE. THE FACILITIES TO BE SOLD UNDER THIS AGREEMENT SHALL BE SOLD ON AN "AS IS - WHERE IS" BASIS. APCO AND APCO'S AFFILIATES MAKE NO WARRANTY OR REPRESENTATION WHATSOEVER, EXPRESS, IMPLIED OR STATUTORY, AND DISCLAIM ANY AND ALL WARRANTIES, INCLUDING, WITHOUT LIMITATION, ANY REPRESENTATION OR WARRANTY AS TO THE VALUE, QUANTITY, QUALITY, CONDITION, SALABILITY, OBSOLESCENCE, MERCHANTABILITY, FITNESS OR SUITABILITY FOR USE OR WORKING ORDER OF ALL OR ANY PART OF SAID FACILITIES. NOTWITHSTANDING THE FOREGOING, AEC SHALL HAVE THE BENEFIT, IN PROPORTION TO AEC'S PERCENTAGE OWNERSHIP INTEREST, OF ALL MANUFACTURERS', VENDORS', AND CONTRACTORS' WARRANTIES AND ALL PATENTS AND LICENSES, IF ANY, RUNNING TO APCO IN CONNECTION WITH THE FACILITIES TO BE SOLD UNDER THIS AGREEMENT, SUBJECT TO THE PROVISIONS OF SECTION 8.03 HEREOF DEALING WITH CONTRACTS WITH THIRD PARTIES. NEITHER AEC NOR AEC'S MEMBERS SHALL HAVE ANY RIGHT OF ACTION AGAINST APCO OR

APCO'S AFFILIATES UNDER ANY THEORY, INCLUDING, BUT NOT LIMITED TO, NEGLIGENCE, STRICT LIABILITY, WARRANTY (EXPRESS OR IMPLIED) BREACH OF CONTRACT, FRAUD OR MISREPRESENTATION, BASED ON THE CONDITION OF THE FACILITIES AT CLOSING.

8.03 Contracts with Third Parties.

(a) Assignment. APCO has acquired or executed, and will in the future acquire or execute, certain contracts, permits, authorizations, licenses, or other intangible rights relating to the Farley Plant. By execution of this Agreement, APCO shall, as of the Closing, be deemed to have granted, conveyed, and assigned to AEC, to the extent permitted by law, contract, or otherwise, an undivided interest in such existing or future contracts, permits, authorizations, licenses, or other intangible rights with respect to the Farley Plant, equal to the Percentage Ownership Interest of AEC, and AEC shall be deemed to have been granted such an undivided Percentage Ownership Interest of the benefits, and to have accepted and assumed a Percentage Ownership Interest of the obligations, of all such contracts, permits, authorizations, licenses, or other intangible rights. AEC agrees to be bound by the terms of all contracts, permits, authorizations, or licenses relating to the Farley Plant (including any provisions that limit or protect against liability, nuclear and non-nuclear, or exclude any warranties) to the same extent as if AEC were an original signatory to such contract, permit, authorization or license or otherwise a party thereto.

(b) Acceptance of Contract Provisions. APCO in such contracts has agreed to certain matters including, but not limited to, limitations on the liability of such contractors for work performed or materials furnished, restrictions on warranties, agreements to indemnify the contractors from liability and other provisions. AEC waives any claims against APCO for having entered into such contracts or agreed to the provisions thereof. AEC also recognizes that a number of the APCO contracts relating to the Farley Plant contain provisions that require APCO to obtain from any assignee or transferee prior to any assignment of rights under such contract or any transfer of materials, equipment or work product, or any interest therein obtained by APCO pursuant to such a contract, an agreement by such assignee or transferee that it will be bound by all of the requirements for financial protection, waivers, releases, indemnifications, limitations of liability and further transfers or assignments that bind APCO under such contracts. AEC agrees that it will be so bound by the requirements for financial protection, waivers, releases, indemnification, limitation of liability and further transfers that bind APCO as they now exist or may in the future be with respect to all contracts relating to the Farley Plant or Nuclear Fuel.

(c) Enforcement of Rights Under Contracts. AEC covenants that, without the written consent of APCO, it will not threaten suit or bring suit against third parties or otherwise

make any claim under any contract or arrangement relating to the Farley Plant and AEC recognizes that APCO has complete and exclusive authority, under the Agreements, with respect to all such matters. If AEC desires for suit to be threatened or brought or otherwise for any claim to be made, or desires that such action contemplated by APCO shall not be taken, AEC shall, by written notice to APCO, request APCO so to act or refrain from acting. Upon receipt of such notice the Parties shall arrange for consultation within ten (10) working days thereafter on the questions raised, or such lesser period of time as APCO, in its sole discretion, shall specify in the light of circumstances requiring a more expeditious determination. APCO shall not make its determination until such consultation but such determination by APCO shall be final and binding on AEC.

8.04 Liabilities of the Parties. (a) All liability to third parties other than liability for Willful Misconduct as defined in paragraph (b) hereof, whether arising in contract (including breach of warranty), tort (including fraud, negligence, strict liability, breach of fiduciary duty or any other theory of tort liability), under the laws of real property or otherwise, or as a result of fines or other penalties imposed by NRC or any other federal or state agency, which results from or is in any way connected with construction, operation, maintenance, modification, or decommissioning of the Facilities shall be shared and apportioned between APCO and AEC in

proportion to their respective Percentage Ownership Interests. To the extent of their respective Percentage Ownership Interests, APCO and AEC each shall indemnify and hold harmless the other, their agents, servants, employees, affiliates or insurers from and against any and all claims, losses, damages, expenses and costs of any kind, other than those attributable to Willful Misconduct of either APCO or AEC as defined in paragraph (b) hereof, whether direct or indirect, on account of or by reason of bodily injuries (including death) to any person or persons or property damage arising out of or occurring in connection with the construction, operation, maintenance, modification or decommissioning of the Facilities, whether or not such claims, losses, damages, expenses or costs were caused by or alleged to have been caused by or contributed to by the active, passive, affirmative, sole or concurrent negligence or by breach of any statutory or other duty (whether non-delegable or otherwise) of APCO or AEC or their agents, servants, employees or affiliates.

Except as expressly authorized in this paragraph (a) and by the provisions of the Basic Agreements, APCO and AEC and their affiliates, servants, employees, agents and insurers hereby release, acquit and forever discharge the other, their agents, servants, employees, affiliates and insurers from any and all claims, causes of action, damages or expenses of whatever kind or nature, which are in any manner connected with the design, engineering, construction, operation, modification

or decommissioning of the Facilities, whether arising in tort (including fraud, negligence, strict liability, breach of fiduciary duty or any other theory of tort liability), contract (including breach of warranty), under the laws of real property or otherwise, or as a result of any fine or other penalty imposed by NRC or any other federal or state agency.

(b) As used in this Agreement, the term Willful Misconduct shall mean any act or omission by APCO or AEC or their affiliates, agents, servants or employees, which is performed or omitted consciously with actual knowledge that such conduct is likely to result in damage or injury to persons or property; provided, however, that no such act or omission, if performed or omitted by an employee, servant, agent, or affiliate of a party, shall be deemed Willful Misconduct of a party unless an employee or officer of such party at or above the level of Vice President in the case of APCO or _____ in the case of AEC shall have expressly authorized such act or omission.

Liability attributable solely to the Willful Misconduct of either APCO or AEC shall not be shared pro rata in accordance with paragraph (a) hereof but shall instead be borne by the party committing such willful act or omission. All other misconduct of any kind or nature shall be apportioned between the parties in accordance with paragraph (a) hereof.

(c) Notwithstanding paragraphs (a) and (b) hereof, in no event shall either party or their affiliates be liable to the other party for any indirect, special, incidental or consequential damages including, without limitation, (1) loss of profits or revenues, (2) damages suffered as a result of the loss of the use of its power system, production facilities or equipment, (3) cost of purchase of replacement power (including any differential in fuel costs), (4) cost of capital, or (5) any other damages resulting from non-operation of the Facilities with respect to any claim based on or in any way connected with the Basic Agreements whether arising in contract (including breach of warranty), tort (including fraud, negligence, strict liability, breach of fiduciary duty or any other theory of tort liability), under the laws of real property or otherwise, or as a result of any fine or other penalty imposed by NRC or any other federal or state agency.

AEC shall indemnify and hold harmless APCO and APCO's affiliates from and against any claim by the AEC Members or member-consumers of AEC Members for any such indirect, special, incidental or consequential damages arising out of any performance or failure to perform under the Basic Agreements. APCO shall indemnify and hold harmless AEC from and against any claim by APCO's customers (other than AEC or AEC Members) for any such indirect, special, incidental or consequential damages arising out of any performance or failure to perform under the Basic Agreements.

ARTICLE IX

General Covenants

9.01 Covenants to Provide Information. Each of the Parties will, from time to time, provide such information as the other Party may reasonably require in connection with the issuance or sale of any bonds or securities or evidences of indebtedness, whether public or private. Each Party further agrees that it will make available to the other Party, upon reasonable request, then-current architectural and construction engineering reports, if any, setting forth the design of the Facilities, the status of any required licenses and permits, estimates of construction costs and construction schedules and reports on the operation of the Facilities.

9.02 AEC's Covenant to Obtain Financing. AEC has applied to REA for guarantees of loans adequate for the permanent financing of AEC's Percentage Ownership Interest in the Facilities. AEC agrees to pursue such application diligently and to use its best efforts to obtain this or other adequate permanent financing and to close by December 31, 1984. Upon granting of the REA loan guarantee commitment, AEC covenants and agrees to accept such loan guarantee commitment and to take all steps within its power to issue bonds or other securities or other evidences of indebtedness, or otherwise to obtain sufficient funds in a timely manner, in order to provide the amounts due from and payable by AEC at the Closing

under the terms of the Basic Agreements. AEC further covenants and agrees that at all times it will use its best effort to obtain sufficient funds in a timely manner, on terms satisfactory to AEC in its reasonable and good faith judgment, to fulfill its obligations under the Basic Agreements. AEC further covenants and agrees that it shall take no action that would prevent, hinder or delay the issuance of any bonds or other securities or evidence of indebtedness, and that it will make all payments and perform all obligations required of it under the indentures or other instruments relating to such bonds or securities or evidences of indebtedness. AEC further covenants and agrees that it shall not incur, create, assume or permit to exist any Lien for borrowed money upon any of the Facilities unless each creditor secured by such Lien has theretofore agreed in a writing addressed to APCO that (a) any interest acquired by APCO in the Facilities, pursuant to either Section 15.02 or 16.01 as a result of a Section 15.02 Event of Default, shall be released by such creditor from, and shall be free and clear of, such Lien upon (i) payment of the purchase price to AEC as provided in Section 15.02(c), in the case of a purchase, or (ii) notice to AEC as provided in Section 16.01, in the case of an automatic adjustment of AEC's Percentage Ownership Interest.

9.03 Financial Statements and Other Documents. (a) APCO covenants and agrees that it will furnish to AEC promptly

after the same are available, copies of all such proxy statements, financial statements and reports as APCO shall send to the holders of its Common Stock and copies of all regular and periodic reports that APCO may file with the SEC.

(b) AEC covenants and agrees to furnish APCO promptly after the same are available, copies of all annual and periodic financial reports that AEC may file with the Alabama Department of Finance, REA or FERC or shall send to the AEC Members, including proxy statements or the equivalent thereof. In addition, AEC shall furnish APCO promptly with copies of all draft agreements and executed agreements relating to the arrangements referred to in Section 9.02.

9.04 Other Covenants. (a) Each Party covenants and agrees that if any event shall occur or condition shall exist which constitutes, or which after notice, lapse of time, or both, would constitute an Event of Default hereunder, it shall immediately (and thereafter on a prompt, continuing basis) notify the other Party thereof, specifying the nature of the Event of Default and any action taken or proposed to be taken with respect thereto.

(b) AEC covenants and agrees that at the Closing it will notify APCO in writing of the names and addresses of each trustee under any instruments of indebtedness and it further covenants and agrees that at all times while this Agreement

remains in effect, it will promptly notify APCO in writing of the names and addresses of all substitute or additional trustees.

(c) AEC covenants that so long as any of the Basic Agreements remain in effect, it will not dissolve. AEC further covenants that it will not consolidate or merge with or acquire any other entity unless it has provided APCO with a certificate to the effect that, (i) as a result of such consolidation, merger, or acquisition, the successor formed by or resulting from such consolidation or merger or the transferee to which such sale shall have been made shall be a solvent corporation organized under the laws of the United States of America or a state thereof, (ii) such successor or transferee corporation shall expressly assume in writing all of the obligations of AEC under the Basic Agreements to the same extent as if such successor or transferee corporation had originally executed the Basic Agreements in the place of AEC, (iii) immediately after such consolidation, merger, sale, or transfer, such successor or transferee shall have a credit worthiness and financial capability to perform its obligations under the Basic Agreements substantially equal to the credit worthiness or financial capability of AEC, and (iv) there shall be no Event of Default or event which, with the giving of notice or the lapse of time or both, could become an Event of Default under the Basic Agreements.

(d) Subject to APCO's rights under Sections 3.02, 8.01 and 13.01(b), APCO covenants to use its best efforts to maintain in effect, and to renew when necessary, all NRC permits and licenses required for the ownership and operation of the Facilities.

(e) APCO covenants to permit officers, directors, employees and proper agents of AEC to have access to and to inspect the Facilities at reasonable times; provided (i) AEC shall give APCO advance notice of any visit to the Facilities and to coordinate with APCO to minimize or avoid any interference with APCO's activity at the Facilities, (ii) APCO may require that any such visit be escorted by APCO personnel, and (iii) such visits shall be made in accordance with all APCO, NRC and other governmental agency regulations, procedures and requirements.

ARTICLE X

Waiver of Partition and Other Rights

10.01 Waiver by AEC. AEC, on its own behalf and on behalf of its successors and assigns, hereby waives any right, whether pursuant to statute or common law, to partition the Facilities, or any portion thereof, and any right to petition for sale for division of the Facilities, and such waiver shall continue in effect until the later of (a) the termination of this Agreement pursuant to Section 17.01 during which APCO may

exercise the option provided for in Section 2.07, or (b) December 31, 2084. AEC agrees not to commence during such period any action of any kind seeking any form of partition or sale for division with respect thereto. AEC agrees to incorporate this waiver in all deeds, deeds of trust, and instruments of conveyance relating to the Facilities, whether delivered at the Closing or thereafter.

10.02 Waiver of other Rights of Joint Tenancy. AEC further waives all other incidents of joint ownership, including but not limited to the right to share in profits from the jointly owned property and accounting therefor, right to use or occupy the premises for uses which do not interfere with any joint use being made of the property, and the right to make expenditures for the benefit of the property and associated rights to demand contribution by APCO to AEC as a result of such expenditures. AEC shall enjoy, nevertheless, all rights associated with its joint ownership which are provided for in the Basic Agreements.

10.03 Waiver of Exercise of Eminent Domain. Both parties agree to waive any right to exercise the power of eminent domain that either party may have with respect to the other party's interest in the Farley Plant. The inclusion of this provision of this Agreement does not acknowledge or admit that either party has the right of eminent domain over the other party.

ARTICLE XI

Assignment

11.01 AEC's Right to Assign. This Agreement and the other Basic Agreements shall be binding upon, and shall inure to the benefit of AEC and APCO, and their respective successors and assigns. AEC shall have the right, subject to the last sentence of Section 9.02, to convey a security interest or interests in AEC's Percentage Ownership Interest to the United States Government or any agency thereof solely to secure loans, or bonds or other evidences of indebtedness issued or to be issued by it, if (a) the proceeds from such loans, bonds or evidences of indebtedness are to be used first to meet AEC's due and unpaid obligations under the Basic Agreements, and (b) immediately after the conveyance of any such security interest, the aggregate amount of all Liens then existing against all of AEC's real and personal property, including the Facilities, shall not exceed ninety percent (90%) of the then aggregate fair market value of all AEC's real and personal property, including the Facilities, with such fair market value to be certified by an independent engineer satisfactory to the Parties. In addition, AEC may request APCO to consent to the assignment of AEC's rights under this Agreement to other parties, solely for financing purposes, and APCO agrees that it will not unreasonably withhold its consent, taking into consideration all aspects of the proposed assignment at that time, including but not limited to consideration of the

last sentence of Section 9.02. AEC shall notify APCO in writing as soon as possible after learning that any Lien has been or will be imposed upon AEC's Percentage Ownership Interest or has reason to believe that any such Lien is under discussion with a possible lender or other entity and shall furnish APCO promptly with all draft copies and executed copies relating thereto. In addition, AEC shall have the right to assign the obligations and benefits under the Basic Agreements to the REA, pursuant to law, for the benefit of the AEC Members. No other succession to or assignment of any rights hereunder or under the other Basic Agreements or any rights in the Facilities shall take place without the prior written consent of APCO.

11.02 Restriction on AEC's Rights to Sell or Otherwise Dispose of Facilities. (a) Unless otherwise agreed to in writing by APCO, or as provided in this Section 11.02, AEC shall not have the right to sell or otherwise dispose of any or all of the Facilities to any party other than APCO, its successors or assigns. Should AEC desire to sell or otherwise dispose of any or all of the Facilities, AEC shall notify APCO of such desire in writing. Upon receipt of any such notice, APCO shall have sixty (60) days from receipt of the notice in which to determine whether it wishes to acquire from AEC any percentage of any of the Facilities then owned by AEC. If APCO determines that it wishes to purchase any or all of such Facilities, it shall have the right to do so at the price

determined in accordance with subsection 11.02(b) below. If APCO elects to purchase the Facilities, Closing for such purchase shall be conducted on a date mutually agreeable to the parties, not in excess of ninety (90) days from the date APCO elects to purchase the Facilities. AEC shall convey such Facilities to APCO by statutory warranty deed. If APCO elects not to purchase any or all of the Facilities, AEC may secure offers to purchase from third parties for the acquisition of AEC's interest therein. Such offers must be received by AEC and copies of such offers must be transmitted to APCO within one hundred twenty (120) days after any election by APCO not to purchase. If any offer desired to be accepted by AEC is less than the amount which APCO would have paid under subsection 11.02(b), AEC shall notify APCO of such desire in writing prior to the expiration of such one hundred twenty (120) day period. APCO shall have the right to purchase such Facilities at the price offered by such third party, such election to be made by APCO within sixty (60) days after notice thereof is given by AEC of its desire to sell at such lower price. In the event APCO elects to purchase at such lower price, the sale of such Facilities shall be conducted within ninety (90) days after APCO elects to purchase. In the event an offer desired to be accepted by AEC is more than that which APCO would have paid under subsection 11.02(b), or in the event such offer is lower and APCO elects not to purchase as provided above, AEC shall have the right to sell its Percentage Ownership Interest in the Facilities or portion thereof not

sold to APCO to a third party. In the event any such sale to a third party is not completed within one (1) year after AEC first gives notice of its desire to sell, AEC shall not be entitled to make such sale until the procedure set forth herein has been complied with in full. In the event a sale is made by AEC of its interest to a third party pursuant to the provisions hereof, the same restrictions on alienation or assignment of its interest in the plant shall be applicable to such third party. In no event of sale to a third party shall AEC be relieved of the obligations to be performed by AEC under the Basic Agreements except to the extent such obligations are actually satisfied by the third party to whom such Percentage Ownership Interest is conveyed.

(b) The purchase price for such interest as APCO elects to acquire shall be an amount equal to the aggregate of the purchase price made or owed by AEC with respect to the Facilities or portions thereof to which such election relates, including appropriate allowances for Actual Cost of Funds During Construction of New Investments less the sum of (i) an amount equal to the revenues required (based on the then allowed rate of return for Alabama jurisdictional customers) to support any amount in default (such amount to be stated without taking any depreciation into account) for the entire period of any such default, less an adjustment for any interest theretofore paid on account of the amount in default, (ii) taxes paid by AEC and included in the Purchase Price or

otherwise paid with respect to the Facilities and additional taxes incurred as a result of the repurchase, (iii) depreciation and amortization accrued on the books of account of AEC, comprised of depreciation reflected in the determination of the Purchase Price (but depreciation reflected in the determination of the Purchase Price shall not be deleted a second time in the application of this Subsection (iii)) and depreciation subsequent thereto determined in accordance with the same methodology used by APCO, excluding amortization applicable to taxes reflected in (ii) above, (iv) any amount, including taxes not included in (ii) above, owed by AEC under the Basic Agreements to APCO, (v) any costs or expenses incurred by APCO, excluding the cost of any debt incurred to finance such acquisition, in connection with such purchase and any indebtedness secured by Liens with respect to the interest in the Facilities being acquired and any other obligation assumed or paid by APCO in order to obtain good title, (vi) any retirements applicable to AEC's Percentage Ownership Interest in the Facilities, and (vii) the Decommissioning Adjustment to Transfer Price calculated in accordance with Section 11.03 hereof.

11.03 Decommissioning Adjustment to Transfer Price. With respect to any transfer hereafter of an interest between the parties hereto which alters the Percent Ownership Interest of the parties in any or all of the Facilities, the price at

which such transfer is made shall be adjusted for decommissioning costs associated with such transferred Facility in an amount equal to:

(1) The amount that the acquiring party would have collected for decommissioning costs for the portion of the Facility being transferred had that party been the owner of such Facility being transferred for the period of time that the other party held ownership title to such portion of the Facility; or

(2) Any other amount reasonably determined by the acquiring party to be necessary to cover fully the then current estimate of decommissioning cost associated with the portion of the Facility being transferred during the period of time that the selling party held ownership title to such portion of the Facility being transferred; or

(3) Any amount specified by applicable legislation or regulatory agencies with appropriate jurisdiction which fixes the total exposure of the acquiring party for future liability for nuclear plant decommissioning, such amount to be prorated over the period of time that the selling party held ownership title to such portion of the Facility being transferred.

11.04 APCO's Right to Assign. So long as it shall have obtained all necessary governmental approvals, APCO shall be

free to assign, transfer or convey any or all of its interest in the Facilities and in this Agreement and the other Basic Agreements at any time without the consent of AEC but no such assignment, transfer or conveyance shall diminish AEC's Percentage Ownership Interest or diminish any other rights of AEC or the obligations of APCO hereunder.

ARTICLE XII

Insurance

12.01 General. During the term of this Agreement, APCO will make reasonable efforts to obtain and maintain in force, in the name of the Parties (naming AEC as a named insured), as their interest may appear, insurance covering the Facilities as described in this Article XII.

12.02 Nuclear Property Insurance. APCO shall, during the period of this Agreement, obtain and maintain in force all-risk nuclear property insurance, available from the American Nuclear Insurers (ANI) and Mutual Atomic Energy Reinsurance Pool (MAERP) or Nuclear Mutual Limited (NML) or other equivalent coverage from some other equivalent insurer. The limit and the deductible of such insurance will be the appropriate amounts as determined by APCO and available from the pools or NML or other equivalent insurer and any deductible will be for the account of the Parties as their interest may appear.

12.03 Nuclear Liability Insurance. APCO will carry insurance to cover the legal obligation to pay damages because of bodily injury or property damage caused by the nuclear energy hazard, the policy to be provided by ANI and Mutual Atomic Energy Liability Underwriters (MAELU) or equivalent coverage from some other equivalent insurer. The limits will be in the amounts required by the Atomic Energy Act of 1954, as amended. APCO will continue to carry such insurance against the foregoing risks with coverage and limits as may be required by the Nuclear Regulatory Commission.

12.04 General Liability Insurance. APCO will carry insurance to cover the legal obligations to pay damages because of bodily injury or property damage caused by other than the nuclear energy hazard. The limit and the deductible of such coverage shall be the appropriate amounts as determined by APCO.

12.05 Workmen's Compensation Insurance. APCO qualifies as a self insurer in Alabama but will provide an umbrella policy to cover benefits in excess of its assumed liability for workmen's compensation and employers liability.

12.06 Additional Insurance. In the event APCO at any time or from time to time shall have elected to participate in supplemental insurance programs to cover costs from nuclear risk including decontamination or property damage and other costs

arising therefrom or replacement power costs due to a prolonged outage (including but not limited to the insurance programs then offered by Nuclear Electric Insurance Limited (or any similar successor organization in which APCO is a participant), the costs of such protection shall be in proportion to the ratio of the ratable exposure represented by AEC's Percentage Ownership Interest to the total ratable exposure of the Facilities. In lieu of participating in any such additional insurance coverage which APCO may provide for the Facilities, AEC may secure separate coverage from other sources so long as such separate coverage (a) provides at least as much protection as would have been provided if AEC had participated in APCO's additional insurance coverage, and (b) such separate coverage shall be of equal quality and reliability and shall have been recognized by APCO, in writing, to be satisfactory to it. AEC may, at its sole expense, purchase and take out any additional insurance for its sole use and benefit as AEC may deem appropriate, provided the interests of AEC are not thereby adversely affected. AEC shall advise APCO of the terms of any such additional insurance prior to entering into any contract therefor.

12.07 Waiver of Subrogation - Allocation and Payment of Premiums. All of the insurance policies obtained by either party shall contain waivers of subrogation against the other party, if obtainable from the insurer. The aggregate cost of all insurance, including supplemental coverage as set forth in

Section 12.06 applicable to the Facilities and procured pursuant hereto, shall be considered an operating expense, consistent with the Uniform System of Accounts. The allocation of premiums, taxes on premiums, deductibles, assessments, retrospective premium calls and any other additional insurance shall be in proportion to the ratio of the ratable exposure represented by AEC's Percentage Ownership Interest to the total ratable exposure of the Facilities. In the event that any of the foregoing insurance policies is cancelled by either Party, that Party shall give written notice of such cancellation to the other Party sixty (60) days prior to the effective date of such cancellation.

ARTICLE XIII

Destruction; Condemnation

13.01 Destruction. (a) If the Facilities or any portion thereof should be damaged or destroyed to the extent that the cost of repairs or reconstruction is estimated by APCO to be equal to or less than the aggregate amount of insurance coverage (including any deductible) carried pursuant to Article XII hereof, then, subject to APCO's rights under Sections 3.02 and 8.01, APCO shall, unless otherwise mutually agreed, cause such repairs or reconstruction to be made so that the Facilities or portions thereof shall be restored to substantially the same general condition, character or use as existed prior to such damage or destruction, and APCO and AEC shall share the cost

not reimbursed by insurance in proportion to their respective ownership interests.

(b) If the Facilities or any portion thereof should be damaged or destroyed to the extent that the cost of repairs or reconstruction is estimated by APCO to be more than the aggregate amount of insurance coverage (including any deductible), APCO may cause such repairs or reconstruction to be accomplished, although APCO shall have no obligation to make such repairs or reconstruction if it chooses not to do so. The Parties shall share such costs, if incurred, proportionately to their ownership interests.

(c) Should APCO elect not to repair or reconstruct such Facilities or any portion thereof, AEC shall not have the right to do so but such Facilities or any portion thereof shall be retired.

13.02 Condemnation. During the term of this Agreement, if there shall occur a loss of title to, or ownership of, or use and possession of, the Facilities or any portion thereof, as the result of, or in lieu of, or in anticipation of, the exercise of the right of condemnation or eminent domain pursuant to any law, general or special, the affected Party will promptly give notice thereof to the other Party, generally describing the nature and extent of such proceedings or negotiations. APCO and AEC shall have the right to participate

fully in any such proceedings or negotiations and each Party shall bear its proportionate share of all reasonable costs, fees and expenses incurred in connection with any condemnation proceedings or negotiations. If no Event of Default shall have occurred and be then continuing, all awards and payments received by APCO or AEC on account of any condemnation (less the actual cost, fees and expenses incurred in collection thereof) shall be paid to the Parties in proportion to their respective ownership interests. For purposes of this Agreement, all amounts paid pursuant to any agreement with any condemning authority which has been made in connection with any condemnation proceeding or negotiation shall be deemed to constitute an award on account of such condemnation.

ARTICLE XIV

Force Majeure

14.01 Force Majeure. In addition to all other limitations on liability contained in this Agreement, APCO shall not be liable or responsible for any delay in the performance of, or the ability to perform, any duties or obligations required by the Basic Agreements when such delay in performance or inability to perform results from a Force Majeure occurrence, except that the obligation of either Party to pay money to the other Party in a timely manner is absolute and shall not be subject to the Force Majeure provisions. Force Majeure as used herein

shall mean any event or cause which is not within the reasonable control of APCO including, without limitation, the following: Acts of God, strikes, lockouts or other industrial disturbances; acts of public enemies; orders, or absence of necessary orders and permits of any kind which have been properly applied for, from the Government of the United States or from any state or territory, or any of their departments, agencies or officials, or from any civil or military authority; extraordinary delay in transportation; inability to transport, store, reprocess or dispose of spent nuclear fuel; unforeseen soil conditions; equipment, material, supplies, labor or machinery shortages; failure of suppliers to conform to obligations in a timely fashion; epidemics; landslides; lightning, earthquakes; fire; hurricanes; tornadoes; storms; floods; washouts; drought; war; civil disturbances; explosions; breakage or accident to equipment, machinery, transmission lines, pipes or canals; failure of Nuclear Fuel assemblies; partial or entire failure of utilities; breach of contract by any supplier, contractor, subcontractor, laborer or materialman; sabotage; injunction; blight; famine; blockade; or quarantine.

14.02 Remedy. If APCO suffers an occurrence of Force Majeure, it shall remedy with all reasonable dispatch the cause or causes preventing APCO from carrying out its agreement; provided, that the settlement of strikes, lockouts and other industrial disturbances shall be entirely within the

discretion of APCO, and it shall not be required to make settlement of strikes, lockouts or other industrial disturbances by acceding to the demands of the opposing party or parties when such course is unfavorable in the judgment of APCO.

ARTICLE XV

Default

15.01 Events of Default. Each of the following shall be "Events of Default" under the Basic Agreements:

(a) The failure by AEC to make any payment then due as required by any of the Basic Agreements within ten (10) days of the date when such payment became due.

(b) Failure by AEC to perform any other obligation to APCO, other than obligations for the payment of money, provided that AEC shall have been given not less than sixty (60) days' notice by APCO of such failure and AEC shall have failed to correct such breach of its obligation or shall have failed to use its reasonable best efforts to correct such breach of its obligations. In the event, notwithstanding such efforts, AEC is unable to correct such breach of its obligations within one hundred twenty (120) days, an Event of Default shall be considered to have occurred.

(c)(i) The insolvency or bankruptcy of AEC or its inability or admission in writing of its inability to pay its debts as they mature, or the making of a general assignment for the benefit of, or entry into any composition or arrangement with, its creditors, other than AEC's mortgagee; or

(ii) The application for, or consent (by admission of material allegations or a petition or otherwise) to, the appointment of a receiver, trustee or liquidator for AEC or for all or substantially all of its assets, or its authorization of such application or consent, or the commencement of any proceeding seeking such appointment against it without such authorization, consent or application, which proceedings remain undismissed or unstayed for a period of sixty (60) days; or

(iii) The authorization or filing by AEC of a voluntary petition in bankruptcy or application for, or consent (by omission of material allegations of a petition or otherwise) to the application of any bankruptcy, reorganization, readjustment of debt, insolvency, dissolution, liquidation or other similar law of any jurisdiction, or the institution of such proceedings against AEC without its authorization, application or consent, which proceedings remain undismissed or unstayed for sixty (60) days, or which result in adjudication of bankruptcy or insolvency within such time.

(d) The willful failure by AEC to pay any amount when due under any obligation to a third party (other than an obligation for borrowed money) incurred in connection with AEC's performance under the Basic Agreements, and such failure shall continue for thirty (30) days thereafter (or if such payment is being contested in good faith, for thirty (30) days after the resolution of such contest).

(e) The failure by AEC to pay any amount when due under any obligation to a third party for borrowed money incurred in connection with the financing of AEC's performance under the Basic Agreements, and such failure shall permit the third party to whom such amount is owed to accelerate such obligation or otherwise to exercise legal or equitable remedies against AEC.

(f) If any representation or warranty made by AEC in the Basic Agreements or any other document or instrument between AEC and APCO securing the Basic Agreements shall not be true and correct in all material respects as of the date when made.

15.02 Remedies for Late Payments. (a) Failure of AEC to make any payment on the date required under the Basic Agreements shall obligate AEC then to pay APCO (i) the unpaid amount, (ii) interest on the unpaid amount at the Special Interest Rate from the date such payment was due until the amount is paid, (iii) the expenses incurred by APCO in

collecting the unpaid amount including but not limited to the expenses of counsel, and (iv) any other expenses incurred by APCO because of the delay such as cost of replacement power because of the inability to operate the Facilities because of such late payment.

(b) Should AEC's failure to make payment not be cured by payments required under Section 15.02(a) above within ten (10) days from the date such payment was due, in addition to incurring penalties under Section 15.02(a), AEC's rights to the available capacity from its Percentage Ownership Interest in the Facilities shall be subject to the option specified in Section 15.04.

(c) If AEC shall fail to make any payments due to APCO after Closing under the Basic Agreements and if such failure shall have continued for a period of forty-five (45) days (including any applicable grace period) without all sums then due (plus interest and penalties due within such forty-five (45) day period) having been paid to APCO, there shall then exist a Class 1 Event of Default. If at the time of or during the continuation of any Class 1 Event of Default, APCO, either by itself or in conjunction with others, shall have the following rights which may not be defeated by any offer or tender made in an attempt thereafter to cure the default.

(i) APCO shall have the right (but shall not be required) to purchase, free and clear of all liens and encumbrances, the entire AEC Percentage Ownership Interest in the Facilities or any percentage of any of the Facilities then owned by AEC. The purchase price for such interest shall be an amount equal to the aggregate of the purchase price paid by AEC applicable to the Facilities to be acquired from AEC, including, with respect to New Investments in the Facilities, appropriate allowances for Actual Cost of Funds During Construction (which Actual Cost shall have been determined using rates no higher than the rates used by APCO for the same period) less the sum of (i) an amount equal to the revenues required (based on the then allowed rate of return for Alabama jurisdictional customers) to support the amount in default (such amount to be stated without taking any depreciation into account) for the entire period of the default, less an adjustment for any interest theretofore paid on account of the amount in default, (ii) taxes paid by AEC and included in the Initial Purchase Price or otherwise paid with respect to the Facilities and additional taxes incurred as a result of the repurchase, (iii) depreciation and amortization accrued on the books of account of AEC, comprised of depreciation reflected in the determination of the Purchase Price (but depreciation reflected in the determination of the Purchase Price shall not be deleted a second time in the application of this Subsection (iii)) and depreciation subsequent thereto determined in accordance with the same methodology used by APCO, excluding

amortization applicable to taxes reflected in (ii) above, (iv) any amount, including taxes not included in (ii) above, owed by AEC under the Basic Agreements to APCO, (v) any costs or expenses incurred by APCO, excluding the cost of any debt incurred to finance such acquisition, in connection with such purchase and any indebtedness secured by Liens with respect to the interest in the Facilities being acquired and any other obligation assumed or paid by APCO in order to obtain good title, (vi) any retirements applicable to AEC's Percentage Ownership Interest in the Facilities, and (vii) the Decommissioning Adjustment to Transfer Price calculated in accordance with Section 11.03 hereof.

(ii) Upon exercise by APCO of its right to purchase AEC's Percentage Ownership Interest in the Facilities pursuant to Section 15.02(c), (i) APCO shall give notice of such election in writing to the trustee or trustees (as named by AEC pursuant to Section 9.04(b) hereof) of AEC's bonds or of other evidences of indebtedness, and (ii) APCO (and where applicable, any other purchasers) shall then be deemed to have purchased AEC's Percentage Ownership Interest in the Facilities, free and clear of all liens and encumbrances, and shall be entitled to all of AEC's rights in the Facilities. Any purchase of AEC's Percentage Ownership Interest in the Facilities pursuant to this Section 15.02(c) shall be subject to the obtaining of applicable governmental and regulatory approvals (other than REA) and AEC shall take all necessary

actions and shall execute, and file where appropriate, all legal documents that shall reasonably be requested by APCO to complete any transaction contemplated by this Section 15.02(c).

(iii) A closing to consummate the purchase by APCO pursuant to this Section 15.02(c) shall be held at a time and place to be determined by APCO.

(d) Should AEC's failure to make payments not be cured by payments under Section 15.02(a), within ten (10) days APCO may exercise its rights under Section 16.01.

15.03 Acceleration. If an Event of Default under Section 15.01 shall have occurred, the entire unpaid amounts owing to APCO, together with any accrued and unpaid interest thereon, shall become immediately due and payable without the necessity of any action by APCO.

15.04 Impact of Default on Entitlement to Capacity until Cure. If any Event of Default has occurred, in addition to other remedies and the Special Remedy provided in Section 16.01, AEC shall not be entitled to the available capacity from its Percentage Ownership Interest in the Facilities. During any period this remedy is in effect, AEC shall continue to be responsible to APCO for any cost of AEC's Percentage Ownership Interest due to be paid to APCO, including operating

costs and cost of New Investments under the Operating Agreement and cost of Nuclear Fuel under the Nuclear Fuel Agreement. At APCO's option, (i) the continuing costs may be foregone by APCO's exercise of its Special Remedy set forth in Section 16.01 with respect to such continuing costs, or (ii) APCO may utilize the energy associated with the available capacity from AEC's Percentage Ownership Interest and credit AEC with the amount of energy so utilized times APCO's average cost of energy from the Farley Plant during the six (6) months preceding the month in which the default occurred; however, in the event unusual circumstances have caused such cost not to represent normal operation, such average cost shall be adjusted downward to reflect energy costs expected during normal cperation.

15.05 Remedies Not Exclusive. If an Event of Default under Section 15.01 shall have occurred, the rights and remedies provided in this Article XV shall not be exclusive but shall be in addition to any other remedy available under the Basic Agreements and, to the extent permitted by law, be cumulative and in addition to all other rights and remedies existing at law, in equity or otherwise, including the right to enforce performance or to recover damages by appropriate proceedings, judicial, administrative or otherwise. In addition, APCO shall have the right to offset any and all amounts owed while any such Event of Default is continuing. No delay or omission to exercise any rights or remedy shall impair such right or

remedy or constitute a waiver of the default or an acquiescence therein. Every right and remedy given by the Basic Agreements, by law or in equity or otherwise, may be exercised from time to time, and as often as may be deemed expedient, by APCO.

ARTICLE XVI

Special Remedies

16.01 Special Remedy. If there exists any default by AEC pursuant to Section 15.01(a), or circumstances described in Section 15.04, then, upon notice to AEC by APCO, at APCO's option, AEC's Percentage Ownership Interest in the Facilities shall automatically be adjusted in accordance with the following formula, applied separately to each of the Facilities, to wit, Farley Unit 1, Farley Unit 2, Common Facilities, and the Operating Inventory:

$$(F)AOI = (F)OI \times \frac{(B-A)}{B}$$

Where (F)AOI equals the adjusted AEC's Percentage Ownership Interest in any of the Facilities, immediately subsequent to the cumulative adjustment effected by this Section 16.01;

(F)OI equals AEC's Percentage Ownership Interest in any of the Facilities at Closing;

A equals the cumulative aggregate amount of all payments then owed (or previously owed to APCO and which were previously a component of A under this

formula) to APCO under Article III or Section 15.03 hereof, including interest at the Interest Rate due thereon for the entire period of the default less taxes owed to APCO with respect to amounts then owed pursuant to Article III or operating or maintenance expenses under any other Agreement between the parties; and

B equals AEC's initial purchase price paid pursuant to Section 3.01 plus the aggregate amount of all payments previously made and the amounts then owed pursuant to the Operating Agreement for New Investment including appropriate allowances for Actual Cost of Funds During Construction (determined in accordance with the provisions of Section 15.02(c)(i) less the sum of the following:

(i) amounts AEC may have paid as penalties, if any have been previously included in this item B; (ii) depreciation and amortization accrued to the books of account of AEC applicable to the Facilities, comprised of depreciation reflected in the determination of the Initial Purchase Price (but depreciation reflected in the determination of the Initial Purchase Price shall not be deleted a second time in the application of this Subsection (ii) and depreciation subsequent thereto determined in accordance with the same methodology used by

APCO, excluding depreciation and amortization applicable to all taxes reflected in (ii) above, and (iii) any retirements applicable to AEC's Percentage Ownership Interest in the Facilities.

Thereafter, each successive Event of Default covered under this Section in any month shall similarly further decrease AEC's Percentage Ownership Interest in the Facilities, unless and until APCO shall have exercised its right to purchase AEC's Percentage Ownership Interest pursuant to Section 15.02.

16.02 Rights and Obligations upon Repurchase or Transfer of Title. (a) In the event of any transfer of or purchase of or adjustment of ownership interest pursuant to this Agreement, AEC shall execute and deliver further documents of title (conforming to the document requirements of Section 2.01) conveying to APCO the interest in the Facilities required by this Agreement, free and clear of all liens and encumbrances, but subject to payment or assumption as provided in the last sentence of Section 9.03.

(b) In the event of any adjustment of ownership interest pursuant to this Article XVI, (i) any loss or expenses incurred by APCO in connection with such acquisition shall be due to APCO from AEC, (ii) APCO shall give notice of such election in writing to the trustee or trustees of AEC's bonds or other evidences of indebtedness, and (iii) a closing to

consummate the acquisition pursuant to this Article shall be promptly held at a time and place determined by APCO.

(c) Any acquisition pursuant to this Article shall be subject to the obtaining of applicable governmental and regulatory approvals and AEC shall take all necessary actions and shall execute, and file where appropriate, all legal documents that shall reasonably be requested by APCO to complete any transaction contemplated by this Article XVI.

ARTICLE XVII

Term of Agreement

17.01 Termination. This Agreement shall terminate at the earlier of (a) when, at the sole judgment of APCO, all the Facilities shall have been retired and decommissioned, when all payments required have been made, when all liability for disposal of waste has terminated, when the plant site has been returned to a condition acceptable to APCO (or when the Parties have entered into a final, definitive, further agreement providing for the permanent care of the Facilities, as permitted by such Section 3.02), and when APCO's option to purchase AEC's Percentage Ownership Interest pursuant to Section 3.02 hereof shall have expired, (b) December 31, 2100, or (c) December 31, 1984 if the Closing shall not have been consummated.

17.02 Measuring Lives. If and to the extent that any of the rights and privileges granted under the provisions of this Agreement would, in the absence of the limitation imposed by this Section, be invalid or unenforceable as being in violation of the rule against perpetuity or any other rule of law relating to the vesting of interests in property or the suspension of the power of alienation of property, then it is agreed that notwithstanding any other provision of this Agreement, said options, rights and privileges, subject to the respective conditions governing the exercise of such options, rights and privileges, shall be exercisable only during (a) a period which shall end twenty-one (21) years after the death of the last survivor of the officers and members of the Board of Directors of APCO named in Exhibit __ hereto, together with all such persons' children and grandchildren who are living on the date of the execution of this Agreement, or (b) the specific applicable period of time expressed in this Agreement, whichever is shorter.

ARTICLE XVIII

Accounting Matters

18.01 General Accounting Matters. Determinations by APCO on all accounting matters related to the transactions contemplated by the Basic Agreements will be in accordance with Generally Accepted Accounting Principles and FERC's Uniform

System of Accounts, utilizing the accrual method of accounting, unless otherwise specifically provided in the Basic Agreements or mutually agreed by the Parties or as prescribed by other regulatory agencies having jurisdiction, as in effect from time to time. The accounting system and procedures designed to implement and operate this Agreement and the other Basic Agreements will be developed with APCO's resources and/or through a consultant. All costs incurred for the design, development and initial implementation of this system are to be borne by AEC.

18.02 Right to Inspect Records, Etc. During normal business hours and subject to conditions consistent with the conduct by APCO of its regular business affairs and responsibilities, APCO will provide AEC, the Authorized AEC Representative(s) or any auditor utilized by AEC reasonably acceptable to APCO or any nationally recognized accounting firm retained by AEC, access to APCO's books, records, and other documents directly related to the performance of APCO's obligations under the Basic Agreements (but excluding internal memoranda, records and documents relating to such matters and minutes of meetings of the Board of Directors and committees thereof) and, upon request, copies thereof, which set forth (a) costs applicable to the construction, operation, maintenance and retirement of the Facilities to the extent necessary to enable AEC to verify the costs for which AEC is billed pursuant to the provisions

of this Agreement, (b) matters relating to the design, construction and operation and retirement of the Facilities in proceedings before any regulatory body or governmental agency having jurisdiction. AEC will bear the cost of any copying, review or audit of such books and records.

During normal business hours and subject to conditions consistent with the conduct by AEC of its regular business affairs and responsibilities, AEC will provide APCO, the Authorized APCO Representative(s), or any auditor utilized by APCO reasonably acceptable to AEC or any nationally recognized accounting firm retained by APCO, access to AEC's books, records, and other documents, and, upon request, copies thereof, which relate to the Basic Agreements (but excluding internal memoranda, records and documents relating to such matters and minutes of meetings of the Board of Directors and committees thereof). APCO will bear the cost of any copying, review or audit of such books and records. Notwithstanding the foregoing, however, neither Party shall be required to make available to the other Party any reports and information relating to personnel practices, staffing or labor relations (including internal memoranda, records and documents relating to such matters as minutes of meetings of the Board of Directors and committees thereof).

18.03 Other Audits. AEC recognizes that APCO is subject to audits by various Federal and State regulatory agencies.

Should any adjustment be required by such audit which affects the Purchase Price or New Investment under this Agreement, the Parties agree to share such adjustment in proportion to their respective ownership interests. AEC also agrees to pay its pro rata share of legal and other expenses incurred by APCO in appealing any adjustment resulting from any such audit, which affects the Purchase Price or New Investment under this Agreement. Any decision to appeal shall be subject to the provisions of Article VIII hereof.

ARTICLE XIX

Consultations and Mutual Cooperation; Authorized Representatives

19.01 Consultations and Mutual Cooperation. At least annually APCO will meet with representatives of AEC at 600 North 18th Street, Birmingham, Alabama, or such other place as the Parties may agree, to report on the operation of the Facilities.

19.02 Authorized AEC Representatives. At the Closing, AEC shall designate, in writing, not more than two (2) Authorized AEC Representatives to act on its behalf with respect to all matters contemplated by this Agreement. The person or persons so designated by AEC as Authorized AEC Representatives may be changed, in the sole discretion of AEC and from time to time, by at least ten (10) days' prior written notice to APCO.

19.03 Authorized APCO Representatives. At the Closing APCO shall designate, in writing, not more than four (4) Authorized APCO Representatives to act on its behalf with respect to all matters contemplated by this Agreement. Any of the Authorized APCO Representatives may be changed, in APCO's sole discretion and from time to time, by at least ten (10) days' prior written notice to AEC.

ARTICLE XX

Miscellaneous

20.01 Non-Exclusive Sale. APCO shall have the right to sell to others joint interests in any or all of its remaining interest in the Facilities upon such terms and conditions as APCO may choose, but no such sale shall diminish AEC's Percentage Ownership Interest in the Facilities or diminish any other rights and interests of AEC hereunder.

20.02 No Arbitration; Resolution of Disputes. No Party shall have the right to arbitrate any dispute that might arise with respect to any of the Basic Agreements. Any disagreement between the Parties as to their rights or obligations under this Agreement shall first be addressed by consultation between the Authorized APCO Representatives and the Authorized AEC Representatives. In the event such representatives are unable to satisfactorily resolve their disagreement, they shall refer to the matter to their respective management. No dispute as to

the payment of an invoice rendered by either Party pursuant to any of the Basic Agreements shall permit the other Party to delay payment of the disputed invoice, in full, on its payment date. If the invoiced Party shall have paid any such disputed invoice, in full, on or before its payment date and if the Authorized APCO Representatives and the Authorized AEC Representatives, or a court of competent jurisdiction, should later determine that a disputed invoice was for an amount in excess of the correct amount due, then the invoicing Party shall be obligated to refund the difference to the invoiced Party within ten (10) days of such determination with interest at the Regular Interest Rate, if any, upon such amount.

20.03 Notices. Any notice, request, consent or other communication permitted or required by this Agreement (other than payments) shall be in writing and be deemed given when delivered by hand or when deposited in the United States mail, first class, postage prepaid, and if to APCO, addressed to:

Alabama Power Company
P. O. Box 2641
Birmingham, Alabama 35291

Attention: President

With copies to: The Authorized APCO Representatives designed by APCO pursuant to Section 19.03 hereof

and if to AEC, addressed to:

Alabama Electric Cooperative, Inc.
P. O. Box 550
Andalusia, Alabama 36420

Attention: General Manager

With copies to: The Authorized AEC Representatives designated by AEC pursuant to Section 19.02 hereof

unless a different officer or address shall have been designated by either Party by notice in writing to the other Party.

20.04 Holidays, Business Days. Any obligation to perform under this Agreement, including payment obligations, which shall become due on a non-business day shall become due upon the next business day. The term "business day" shall mean any day other than a day on which banking institutions in the City of Birmingham, Alabama are authorized by law to close.

20.05 Entire Agreement. This Agreement, together with the other Basic Agreements, constitutes the entire understanding between the Parties hereto, superseding any and all previous understandings, oral or written, pertaining to the subject matter contained herein and therein. No Party hereto has relied or will rely upon any oral or other written representation or oral or other written information made or given to such Party by any representative of the other Party or anyone on its behalf.

20.06 Amendments. This Agreement may not be amended, modified, or terminated, nor may any obligation hereunder be waived, orally, and no such amendment, modification, termination or waiver shall be effective for any purpose unless it is

in writing, and signed by both Parties and all necessary regulatory approvals, including the Administrator of REA, have been obtained.

20.07 Relationship of the Parties. The duties, obligations and liabilities of the Parties are intended to be several and not joint or collective, and nothing herein contained shall ever be construed to create an association, trust, joint venture or partnership or impose a trust, fiduciary or partnership duty, obligation, or liability on or with regard to the Parties, although the Parties acknowledge that the ownership and operation of the Facilities may constitute a partnership for tax purposes. The Parties shall be individually responsible for their own obligations as provided herein. Neither Party shall have the right or power to bind the ther Party except as expressly provided in this Agreement.

20.08 Tax Election. APCO and AEC hereby agree that they will both elect to exclude the arrangement created by this Agreement from the application of Subchapter K of the Internal Revenue Code of 1954, as amended, and execute all documents required by either Party to effect that result.

20.09 Governing Law. This Agreement is made under and shall be construed under and governed by the laws of the State of Alabama.

20.10 No Waiver. The failure of either Party to enforce at any time any of the provisions of this Agreement, or to require at any time performance by the other Party of any of the provisions hereof, shall in no way be construed to be a waiver of such provisions, nor in any way to affect the validity of this Agreement or any part thereof, or the right of such Party thereafter to enforce each and every such provision.

20.11 Captions. The descriptive captions of the various Articles and Sections of this Agreement have been inserted for convenience of reference only and shall in no way modify or restrict any of the terms and provisions hereof.

20.12 Counterparts. This Agreement may be executed simultaneously in two or more counterparts, each of which shall be deemed an original, but all of which together shall constitute one and the same instrument.

20.13 Singular and Plural; Gender. Throughout this Agreement, whenever any word in the singular number is used, it should include the plural unless the context otherwise requires; and whenever the plural number is used, it shall include the singular unless the context otherwise requires. The use of the masculine shall include the feminine.

20.14 REA Required Clauses - Incremental Cost of Compliance; Remedies for Non-compliance. (A) AEC has represented to APCO

that REA will not loan, or guarantee the loan of, money to AEC for its investment in the Farley Nuclear Plant unless APCO agrees to the inclusion of the provisions set forth as Items (C)(1) through (7) of this Section 20.14. APCO has agreed to the inclusion of these items with the express understanding and agreement (and acknowledgement by REA) that their inclusion is subject to the conditions and limitations set forth in Section 20.14(B) below.

(B)(1) In the event APCO experiences any increase in its costs because of any of the provisions set forth in Section 20.14(C), the entire burden of such increase in cost shall be borne by AEC and AEC shall pay such increase in cost upon receipt of invoice as provided in Article V of the Operating Agreement.

(2) In no event shall any breach by APCO of any of the provisions of Section 20.14(C)(1) through (7) give AEC (or any party claiming rights hereunder through AEC) the right or opportunity to terminate the Basic Agreements or any of them, or diminish the obligations of AEC (or any party claiming rights through AEC) under the Basic Agreements.

(C)(1) Buy American. The parties covenant that in the performance of this Agreement (i) at least AEC's Percentage Ownership Interest in the total cost of the Farley Nuclear Plant, including the total of all of the unmanufactured

articles, materials and supplies used or to be used in the construction of or otherwise made a part of the Farley Nuclear Plant shall have been mined or produced in the United States, and (ii) at least AEC's Percentage Ownership Interest in the total cost of the Farley Nuclear Plant, including the total cost of all of the manufactured articles, materials, and supplies used or to be used in the construction of or otherwise made a part of the Farley Nuclear Plant shall have been manufactured in the United States substantially all from articles, materials, or supplies mined, produced, or manufactured, as the case may be, in the United States. If any article, material, or supplies are partially mined, produced, or manufactured in the United States (said part being hereinafter called the "American Made Portion") and partially mined, produced, or manufactured somewhere other than in the United States, then only the cost of the American Made Portion shall be used in determining whether the requirements of the preceding sentence have been satisfied. At the Closing and from time to time thereafter when requested by AEC or the REA Administrator, the parties shall supply the REA Administrator or the party so requesting with information and documentation demonstrating that the Farley Nuclear Plant was constructed in accordance with the requirements of this Section, provided AEC shall reimburse APCO all costs incurred by APCO in providing such information and documentation, including reimbursement, at usual hourly rates, the cost of the time of personnel engaged in any such supply of information and documentation.

AEC shall further reimburse APCO for any cost which APCO incurs in complying with this provision in lieu of procuring goods or services outside the United States.

(2) Historic Places. The parties shall not, without approval in writing by the REA Administrator, use any portion of the funds made available to APCO by AEC pursuant to the terms of this Agreement to construct any facilities which will involve any district, site, building, structure or object which is included in the National Register of Historic Places, maintained by the Secretary of the Interior pursuant to the Historic Sites Act of 1935 and the National Historic Preservation Act.

(3) Flood Insurance Act. Notwithstanding anything contained in this Agreement, neither party shall be under any obligation to advance any funds to the other party to finance the construction or acquisition of any building in any area heretofore identified by the Secretary of Housing and Urban Development, pursuant to the Flood Disaster Protection Act of 1973 (the "Flood Insurance Act") or any rules, regulations or orders issued to implement the Flood Insurance Act ("Rules"), as an area having special flood hazards, or to finance any Facilities or materials to be located in any such building, or in any building owned or occupied by APCO or AEC located in such flood hazard area unless and until there have been compliance with all other conditions of this Agreement which are

precedent to such advances, and the REA Administrator has determined that (i) the community in which such area is located is then participating in the national flood insurance program, as required by the Flood Insurance Act and any Rules, and (ii) APCO and AEC have obtained flood insurance coverage with respect to such building and contents as may then be required pursuant to the Flood Insurance Act and any Rules, AEC being responsible for the entire cost of any such insurance. In the event, because of this provision, AEC fails to pay for any portion of the Facilities, AEC shall not be entitled to its Percentage Ownership Interest in any output of the Farley Nuclear Plant.

(4) Public Officials Not to Benefit. No member of or delegate to the Congress of the United States shall be admitted to any share or part of this Agreement or to any benefit to arise herefrom other than the receiving of electric service on the same terms accorded other consumers and other than benefits, if any such person is an APCO or The Southern Company shareholder, that may accrue to such shareholders generally.

(5) Kickbacks. In the acquisition, construction and completion of Facilities pursuant to this Agreement, APCO and AEC shall comply with all applicable statutes, rules and regulations pertaining to the so-called "Kickback" Statute (48 Stat. 948, 18 U.S.C. Sec. 874 and 40 U.S.C. Sec. 276C).

(6) Equal Opportunity Clause. During the term of this Agreement, the parties agree as follows:

(i) The parties will not discriminate against any employee or applicant for employment because of race, color, religion, sex, age or national origin. The parties will take affirmative action to ensure that applicants are employed, and that employees are treated during employment without regard to their race, color, religion, sex, age or national origin. Such action shall include, but not be limited to the following: Employment, upgrading, demotion or transfer; recruitment or recruitment advertising; layoff or termination; rates of pay or other forms of compensation; and selection for training, including apprenticeship. The parties agree to post in conspicuous places, available to employees and applicants for employment, notices to be provided setting forth the provisions of this Equal Opportunity Clause.

(ii) The parties will, in all solicitations or advertisements for employees placed by or on behalf of either party, state that all qualified applicants will receive consideration for employment without regard to color, religion, sex, age or national origin.

(iii) The parties will send to each labor union or representative of workers with which it has a collective bargaining agreement or other contract of understanding, a

notice to be provided advising that said labor union or workers' representatives of the parties' commitments under this Section, and shall post copies of the notice in conspicuous places available to employees and applicants for employment.

(iv) The parties will comply with all provisions of Executive Order 11246 of September 24, 1965, and of the rules, regulations and relevant orders of the Secretary of Labor.

(v) The parties will furnish all information and reports required by Executive Order 11246 of September 24, 1965, and by rules, regulations and relevant orders of the Secretary of Labor, or pursuant thereto, and will permit access to their books, records and accounts by the administering agency and the Secretary of Labor for purposes of investigation to ascertain compliance with such rules, regulations and orders.

(vi) In the event of either party's noncompliance with this Equal Opportunity Clause of this Agreement or with any of the said rules, regulations or orders, the party may be declared ineligible for further government contracts or federally assisted construction contracts in accordance with procedures authorized in Executive Order 11246 of September 24, 1965, such being the sole and exclusive remedy applicable

under this Agreement for noncompliance herewith, it being recognized that the parties have executed other Agreements under which broader remedies for such noncompliance has been recognized.

(vii) The parties agree that, unless exempted by the rules, regulations or orders of the Secretary of Labor issued pursuant to Section 204 of Executive Order 11246 of September 24, 1965, all subcontracts and purchase orders are subject to Executive Order 11246 and such provisions will be binding upon each subcontractor and vendor. The parties shall take such action with respect to any subcontract or purchase order as the administering agency may direct as a means of enforcing such provisions, including sanctions for noncompliance; provided, however, that in the event the party becomes involved in, or is threatened with litigation with a subcontractor or vendor as a result of such direction by the administering agency, that party may request the United States to enter into such litigation to protect the interests of the United States.

(7) Nonsegregated Facilities. The parties certify that they do not maintain or provide for their employees any segregated facilities at any of its establishments, and that it does not permit their employees to perform services at any location, under their control, where segregated facilities are maintained. The parties certify further that they will not

maintain or provide for their employees any segregated facilities at any of their establishments, and that they will not permit their employees to perform their services at any location, under their control, where segregated facilities are maintained. The parties agree that a breach of this certification is a violation of the Equal Opportunity Clause in this Agreement and that the sole and exclusive remedy for breach of this certification is the sole and exclusive remedy set forth in the Equal Opportunity Clause of this Agreement. As used in this certification, the term "segregated facilities" means any waiting rooms, work areas, restrooms and washrooms, restaurants and other eating areas, timeclocks, locker rooms and other storage or dressing areas, parking lots, drinking fountains, recreation or entertainment area, transportation, and housing facilities provided for employees which are segregated by explicit directive or are in fact segregated on the basis of race, color, religion, or national origin, because of habit, local custom, or otherwise. The parties agree that (except where they have obtained identical certifications from proposed subcontractors for specific time periods) they will obtain identical certifications from proposed subcontractors prior to the award of subcontracts exceeding $10,000 which are not exempt from the provisions of the Equal Opportunity Clause, and that they will retain such certifications in their files.

IN WITNESS WHEREOF, the parties have hereto caused this Agreement to be signed and sealed as of _____, 1984 by their duly authorized representatives.

ALABAMA POWER COMPANY

By_____

ATTEST:

_____
Corporate Secretary

ALABAMA ELECTRIC COOPERATIVE, INC.

By_____

ATTEST:

_____

STATE OF ALABAMA:
to-wit:
JEFFERSON COUNTY

The foregoing instrument was acknowledged before before me this ____ day of _____, 1984 by _____ and _____, President and Corporate Secretary, respectively, of Alabama Power Company, an Alabama corporation, on behalf of the Corporation.

My commission expires:_____

_____
Notary Public

STATE OF ALABAMA:
to-wit:
COVINGTON COUNTY

The foregoing instrument was acknowledged before me this _____ day of _____, 1984 by _____, of Alabma Electric Cooperative, Inc. an Alabama corporation, on behalf of the Corporation.

My commission expires:_____

_____

EXHIBIT A

COMMON FACILITIES
JOSEPH M. FARLEY NUCLEAR PLANT

[Description to be developed of all facilities at the Farley Plant considered Common Facilities as of the date of the Purchase and Ownership Agreement]

EXHIBIT B

FARLEY UNIT 1
JOSEPH M. FARLEY NUCLEAR PLANT

[Description to be developed of the facilities included within the Farley Plant which constitute Farley Unit 1]

EXHIBIT C

FARLEY UNIT 2
JOSEPH M. FARLEY NUCLEAR PLANT

[Description to be developed of the facilities included within the Farley Plant which constitute Farley Unit 2]

EXHIBIT D

MEMBERS OF ALABAMA ELECTRIC COOPERATIVE, INC.
AS OF _____, 1984

City of Andalusia
Baldwin County Electric Membership Corporation
City of Brundidge
Central Alabama Electric Cooperative
Choctawhatchee Electric Cooperative
Clarke-Washington Electric Membership Corporation
City of Elba
Escambia River Electric Cooperative
Gulf Coast Electric Cooperative
Micolas Cotton Mills
City of Opp
Opp Cotton Mills
Pea River Electric Cooperative
Pioneer Electric Cooperative
South Alabama Electric Cooperative
Southern Pine Electric Cooperative
Tallapoosa River Electric Cooperative
West Florida Electric Cooperative
Wiregrass Electric Cooperative

EXHIBIT E

STATUTORY WARRANTY DEED

[Statutory Warranty Deed to be developed consistent with Section 2.02(a) conveying to AEC an undivided ownership interest in real property to be conveyed under the Agreement]

EXHIBIT F

ASSIGNMENT OF CONTRACTS, LICENSES AND PERMITS

[Document to be developed assigning to AEC, to the extent possible, an undivided ownership interest in APCO's rights and obligations under those certain contracts, licenses and permits listed herein for the purchase, repair, construction, ownership and operation of the Facilities]

EXHIBIT G

BILL OF SALE

[Bill of Sale to be prepared conveying undivided ownership interest in all property listed thereon]

EXHIBIT H

SECOND MORTGAGE AND DEED OF TRUST

[Document to be prepared evidencing second mortgage lien on property of AEC as security for obligations owed by AEC to APCO under the Basic Agreements]

EXHIBIT I

PURCHASE PRICE FOR AEC'S
PERCENTAGE OWNERSHIP INTEREST

[Document to be prepared stating purchase price and showing allocation among the various elements constituting the price]

EXHIBIT J

GUARANTY AGREEMENT

[Guaranty Agreement, binding REA, to be prepared to guarantee AEC's performance of the Basic Agreements]

EXHIBIT K

SPECIAL GUARANTY AGREEMENT

FOR AND IN CONSIDERATION of Ten Dollars ($10.00) and other good and valuable considerations, the receipt and sufficiency of which is hereby acknowledged, the undersigned, for themselves, their successors and assigns (hereinafter "Guarantors"), being members of ALABAMA ELECTRIC COOPERATIVE, INC., a corporation organized under the laws of the State of Alabama (hereinafter "AEC"), hereby each guarantees to ALABAMA POWER COMPANY, its successors and assigns (hereinafter "APCO") full payment and/or performance of all costs, liabilities and obligations of AEC to APCO, including payment of accrued interest if any, arising out of or resulting from that certain Purchase and Ownership Agreement between APCO and AEC dated _____, 1984, that certain Nuclear Fuel Agreement between AEC and APCO dated _____, 1984, and that certain Operating Agreement between AEC and APCO dated _____, 1984 (hereinafter collectively referred to as "Basic Agreements"), to which true copies of this Special Guaranty Agreement are affixed, or arising out of or resulting from a violation by AEC of any of the covenants contained in the Statutory Warranty Deed and Bill of Sale to be delivered by APCO to AEC pursuant to the Basic Agreements ("guaranteed items"). Notwithstanding anything to the contrary herein contained, the liability of each of the undersigned is limited to

that percentage of the entire liability hereunder which is set forth below, as follows:

City of Andalusia	_____%
Baldwin County Electric Membership Corporation	_____%
City of Brundidge	_____%
Central Alabama Electric Cooperative	_____%
Choctawhatchee Electric Cooperative	_____%
Clarke-Washington Electric Membership Corporation	_____%
City of Elba	_____%
Escambia River Electric Cooperative	_____%
Gulf Coast Electric Cooperative	_____%
Micolas Cotton Mills	_____%
City of Opp	_____%
Opp Cotton Mills	_____%
Pea River Electric Cooperative	_____%
Pioneer Electric Cooperative	_____%
South Alabama Electric Cooperative	_____%
Southern Pine Electric Cooperative	_____%
Tallapoosa River Electric Cooperative	_____%
West Florida Electric Cooperative	_____%
Wiregrass Electric Cooperative	_____%

1. This guaranty is unconditional, provided only that each Guarantor may assert any defense that would be available to AEC under the Basic Agreements and that has not been resolved against AEC pursuant to the final decision of a court of competent jurisdiction.

2. This guaranty shall be deemed continuing and irrevocable, notwithstanding any subsequent withdrawal of any or all of the Guarantors as members of AEC, provided that an express release given by APCO to AEC shall also constitute a release of each of the Guarantors hereunder. Guarantors hereby waive demand of payment, presentment, protest and notice of protest on any and all of the guaranteed items and consent to alteration, amendment, or modification of any obligations under the Basic Agreements without necessity for notice to Guarantors or agreement by Guarantors. Payments by the Guarantors to APCO pursuant to this guaranty shall be made at the principal place of business of APCO, in lawful money of the United States.

3. The obligations of each Guarantor may be enforced without regard to the enforcement of the obligations of any other Guarantor, and without regard to the validity or invalidity of any obligations of another Guarantor. Any amounts received by APCO from whatsoever source on account of the AEC's indebtedness or liabilities, and in such order of application, as APCO may from time to time elect; and, notwithstanding any payments made by or for the account of the undersigned pursuant to this guaranty, the undersigned shall not be subrogated to any rights of APCO until such time as this guaranty shall have been discontinued as to all of the undersigned and APCO shall have received payment of the full amount of all indebtedness or liabilities and of all obligations of all of the undersigned hereunder.

4. Guarantors hereby consent to APCO from time to time extending the time of payment or performance in whole or in part of any and all of the aforesaid items for such time or times as APCO may determine and hereby waive notice to or obtaining the consent of the Guarantors. Such extension of extensions may be longer than the time for payment or performance of the original obligation. Guarantors further agree that this guaranty shall apply with equal force and effect to any renewal or renewals of any of the aforesaid items. Guarantors further consent to the subsequent sale by APCO of participation interests in the Farley Plant to persons other than AEC, or to APCO otherwise dealing with the Farley Plant, and agree that such shall not impair this guaranty, and hereby waive notice thereof to or obtaining the consent therefor of the Guarantors. Guarantors hereby consent to the partial or total release of other persons (except AEC) primarily or secondarily liable, and to the release of all or part of any security that may be held by APCO all without notice to Guarantors. APCO shall not be obligated to acquire any security or substitute security because of the release of other security. If at any time all or any part of any payment theretofore applied by APCO to any indebtedness or liability of AEC is or must be rescinded or returned by APCO for any reason whatsoever (including without limitation the insolvency, bankruptcy or reorganization of AEC) such indebtedness or liability shall for the purpose of this guaranty, to the extent that such payment is or must be rescinded or returned,

be deemed to have continued in existence notwithstanding such application by APCO, and this guaranty shall continue to be effective or be reinstated, as the case may be, as to such indebtedness or liability as though such application by APCO had not been made.

5. Notice by APCO of the acceptance of this guaranty is hereby waived. No act or omission of any kind (except express written release of the AEC) by APCO shall affect or impair this guaranty and APCO shall have no duties to the Guarantors. The Guarantors hereby agree that their obligations hereunder shall be absolute and primary and shall be complete and binding as to each Guarantor upon this guaranty being executed by it and subject to no conditions precedent or otherwise. This guaranty contains the full agreement of the Guarantors and is not subject to any oral conditions.

6. No modification or waiver hereof shall be binding on APCO unless in writing signed by an officer of APCO. This guaranty shall be construed in accordance with and governed by the laws of the State of Alabama. Wherever possible each provision of this guaranty shall be interpreted in such manner as to be effective and valid under applicable law, but if any provision of this guaranty shall be prohibited by or invalid under such law, such provision shall be ineffective to the extent of such prohibition or invalidity, without invalidating the remainder of such provision or the remaining provisions of this guaranty.

EXHIBIT L

RELEASE AND COVENANT NOT TO SUE

[Document to be prepared for execution by AEC and each AEC Member, together with certified resolutions of the Board of Directors of each entity authorizing execution]

EYHIBIT M

OPINION OF COUNSEL FOR AEC

EXHIBIT N

OPINION OF COUNSEL FOR AEC

ATTACHMENT 11

OPERATING AGREEMENT FOR JOINT OWNERSHIP INTEREST
IN THE JOSEPH M. FARLEY NUCLEAR PLANT UNITS ONE AND TWO
BETWEEN
ALABAMA POWER COMPANY
AND
ALABAMA ELECTRIC COOPERATIVE, INC.

OPERATING AGREEMENT
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OPERATING AGREEMENT FOR JOINT OWNERSHIP INTEREST
IN THE JOSEPH M. FARLEY NUCLEAR PLANT UNITS 1 AND 2
BETWEEN
ALABAMA POWER COMPANY
AND
ALABAMA ELECTRIC COOPERATIVE, INC.

THIS OPERATING AGREEMENT is made and entered into as of _____, ____, between ALABAMA POWER COMPANY ("APCO"), an Alabama corporation with its principal office at 600 North 18th Street, Birmingham, Alabama, and ALABAMA ELECTRIC COOPERATIVE, INC. ("AEC"), an electric cooperative organized under Alabama law, with its principal office at _____ _____, Andalusia, Alabama.

WHEREAS, APCO, an electric utility organized and existing under the laws of the State of Alabama, has constructed and operates a nuclear plant near Dothan, Alabama, referred to as the Joseph M. Farley Nuclear Plant (the "Farley Plant"), subject to the requirements of the licenses issued by the Nuclear Regulatory Commission; and

WHEREAS, AEC is a generation and transmission cooperative organized and existing under the laws of the State of Alabama; and

WHEREAS, simultaneously herewith, APCO and AEC have entered into a Purchase and Ownership Agreement for Joint Ownership Interest in the Farley Nuclear Plant ("Purchase and Ownership Agreement") and a Nuclear Fuel Agreement, under which APCO will sell and AEC will purchase an ownership

interest in Farley Unit 1, Farley Unit 2, Common Facilities, Operating Inventory and the Nuclear Fuel used or to be used for Farley Units 1 and 2; and

WHEREAS, pursuant to the Purchase and Ownership Agreement, APCO is to sell to AEC a joint interest in the Facilities described in such Agreement and, through this Operating Agreement, has agreed to operate AEC's portion of such Facilities, supplying to AEC such electricity as is generated from AEC's portion of these Facilities; and

WHEREAS, AEC agrees to compensate APCO, in the manner provided herein, for the operation of the Facilities and conduct of other activities including, but not limited to, maintenance, construction, refurbishment, and modification of the Facilities or additions thereto as may be required or desirable.

NOW, THEREFORE, in consideration of the premises and the mutual obligations hereinafter stated, the parties hereto agree to the following Operating Agreement governing the Farley Plant.

ARTICLE I

APCO's Authority and Responsibility with Respect to Operation of AEC's Percentage Ownership Interest

1.01 APCO as Agent of AEC.

(a) AEC hereby reaffirms its appointment of APCO (such appointment to be irrevocable for the term of this

Operating Agreement and coupled with an interest) as its sole agent as provided in Section 8.01 of the Purchase and Ownership Agreement, to act on behalf of AEC with respect to all matters specified in such Section 8.01.

(b) As relates to all third parties, this agency designation shall be binding on AEC, and such appointment shall be deemed in effect by each third party until such third party receives written notification from APCO of any termination thereof.

(c) APCO accepts such appointment. APCO shall have the right to exercise such authority granted to it by AEC through a contractor or agent selected by APCO. In any such event, the authority of such contractor or agent shall be coextensive with the authority granted APCO and such contractor and agent shall be an additional beneficiary of all provisions of this Operating Agreement and the other Basic Agreements including, but not limited to, those relating to responsibility of the operator of the facility and payment of cost. In discharging all of its duties and responsibilities hereunder, APCO will not, solely because of AEC's Percentage Ownership Interest in the Facilities, make any adverse distinction between any of the Facilities and any other generating unit or facilities in which APCO has an ownership interest, provided nothing herein shall require APCO to perform (or make it liable to AEC for performing) in any manner different from the manner it would have performed had AEC not

obtained a percentage ownership in the Facilities. In connection with any claim by AEC that APCO has made an adverse distinction solely because of AEC's percentage ownership, the burden of making such demonstration shall be on AEC. APCO's duties and responsibilities under this Operating Agreement shall include, but not be limited to, establishing organizational structure and manpower requirements, maintaining an adequate work force through APCO's personnel administration policies, arranging and procuring necessary or desirable materials and services for operation of the Facilities, determining scheduled outages for routine inspections, refueling and general maintenance, scheduling, dispatching and loading of the Facilities, preparing and filing applications, reports and other documents relating to operation of the Facilities, establishing reasonable rules for visits to the Facilities, and determining the need for, and subsequently constructing, any capital additions or modifications to the Facilities. Nothing herein shall interfere with APCO's authority and responsibility for the operation of, maintenance of, modifications to, fueling of, and improvements to all of its other generation facilities. APCO shall make available upon request by AEC regularly prepared monthly reports which contain specific information on the Facilities, including, but not limited to, operating expenses, maintenance expenses, fuel expenses, generating statistics, fuel reports, operating statistics, and other information reasonably available. APCO

will also have the right to submit data relating to operation of the Facilities to any other entity. APCO shall also provide AEC oral notice of scheduled and emergency outages of Farley Unit 1 or Farley Unit 2 in a manner and at times convenient to APCO. Should AEC desire to have capability for determining automatically the current level of generation at the Farley Plant, AEC shall bear the full cost incurred by APCO on installing, operating, and maintaining equipment necessary to provide such capability and shall reimburse APCO for any cost expended by APCO in connection therewith.

(d) AEC agrees that it will take all necessary action in a prompt manner to execute any agreements with respect to the operation, maintenance, modifications and fueling of the Facilities as and when requested by APCO to permit APCO to carry out its authority and responsibilities pursuant to this Section 1.01.

(e) AEC expressly agrees that APCO does not, by this Operating Agreement, assume any risks or liabilities with respect to AEC's Percentage Ownership Interest and that the amounts paid and payable to APCO under the Basic Agreements are determined on the basis that APCO does not assume any such risks or liabilities.

1.02 AEC's Review of Plant Activities. APCO shall, upon receipt of reasonable notice from AEC in advance, make arrangements for visitation by representatives of AEC at the plant provided such visits shall not, in the sole opinion of

APCO, interfere with APCO's operation of the plant or jeopardize plant safety. During any such visit by AEC representatives, APCO personnel may accompany such AEC representatives at all times. AEC shall assure that its representatives comply with all applicable rules and regulations in effect at the Farley Plant whether imposed by governmental authority or by APCO.

ARTICLE II

Entitlements to Output

2.01 Entitlements of the Parties to Output. Subject to the provisions of Articles XI, XV and XVI of the Purchase and Ownership Agreement, AEC shall be entitled to its Percentage Ownership Interest of the output from Farley Units 1 and 2 at the time generation in such units occurs. Subject to the provisions of Articles XI, XV or XVI of the Purchase and Ownership Agreement, APCO shall be entitled to the balance of the output from each unit.

2.02 Determination of Output - Responsibility for Station Service and Losses. Output of the Farley Plant shall be the gross generation of Farley Units 1 and 2, less station service requirements, and less adjustments for losses experienced. In the event the output is negative, that is, the station service and losses exceed the gross generation, AEC shall pay APCO for its share of the energy consumed or lost at the plant during such period on the basis of APCO's incremental energy cost at that time.

ARTICLE III

Delivery of Power

3.01 Delivery of Power. APCO shall deliver to AEC the output to which it is entitled under Article II, such delivery to be made at the points where the 500 and 230 kilovolt transmission lines connect to bus bars in the transmission substation at the Farley Plant. Transmission of such output by APCO for AEC shall be governed by the provisions of a separate agreement.

3.02 Metering.

(a) No special metering shall be installed at the Farley Plant, it being understood that the output to which AEC is entitled pursuant to Article II hereof shall be determined by appropriately adjusting the metered quantities to reflect the capacity and energy delivered to AEC at the point of delivery described in Section 3.01. AEC shall bear the costs of any additional metering or data acquisition equipment which is required to measure accurately the delivery of power to AEC from the Farley Plant.

(b) The meters will be sealed and seals will be broken only by APCO and only when meters are to be tested or adjusted. The meters will be tested at suitable intervals and the accuracy of registration shall be maintained. At AEC's request, a special test of any meter will be performed. All costs of such a test will be borne by AEC. Representatives of AEC shall be afforded the opportunity to be present at all routine or special tests.

ARTICLE IV

Costs

4.01 Operating Costs. On or before the first day of January of each year during the term of this Operating Agreement, APCO shall provide to AEC a monthly estimate of operating costs for the twelve (12) month period commencing on that January 1. APCO will also provide to AEC, upon request, such estimates of operating costs for future years as APCO shall have prepared for its own use. The estimate shall not be binding on APCO but shall be provided solely to assist AEC in planning. During the term of this Operating Agreement, AEC shall pay to APCO its pro rata share of the costs of operating and maintaining the Facilities in accordance with Appendix A hereto. The pro rata share of AEC shall be subject to change from time to time in accordance with Articles XI, XV or XVI of the Purchase and Ownership Agreement. The operating costs shall be paid on an estimated basis as provided in Article V hereof, subject to adjustment based on actual cost.

4.02 New Investment Costs.

(a) On or before the first day of January of each year during the term of this Operating Agreement, APCO shall provide to AEC a monthly estimate of New Investment for the twelve (12) month period commencing on that January 1. APCO will also provide to AEC, upon request, such estimates of New Investment for future years as APCO shall have prepared for its own use. The estimate shall not be binding on APCO but

shall be provided solely to assist AEC in planning for its capital requirements.

(b) At the times specified in Section V hereof, APCO will submit an invoice to AEC for its share (as provided in Section 4.02(d) below) of the next month's estimated expenditures for New Investment. Such cost will be as described in Appendix B hereto. When the actual expenditures for New Investment for that month have been determined by APCO and recorded on its books of account, an adjustment shall be made by APCO to reflect a credit or additional charge to AEC.

(c) APCO shall also furnish AEC monthly, in addition to the estimate of expenditures for New Investment during the next month, the then current estimates of the New Investment for each of the remaining months in that calendar year (unless there is no change), which estimates may be different from the monthly estimate originally furnished on or before January 1 pursuant to Section 4.02(a). The delivery of such estimates (which estimate shall not be binding upon APCO but shall be provided solely to assist AEC in planning for its capital requirements) of New Investment for the remaining months of the calendar year shall constitute notice by APCO to AEC of any change in APCO's estimate. APCO agrees, however, to use reasonable efforts to give AEC as much advance notice of New Investment estimate changes as is practicable, particularly in the case of changes which may substantially increase the amount AEC must pay for its share of New Investment in a future month.

(d) AEC's share of New Investment to be paid to APCO each month shall be a percentage of New Investment for such month equal to AEC's Percentage Ownership Interest in the Facilities as such specified Percentage Ownership Interest shall be modified in accordance with the provisions of Articles XI, XV or XVI of the Purchase and Ownership Agreement.

4.03 Incremental Costs. Any incremental costs due to be paid by AEC under any of the Basic Agreements after Closing shall be paid by AEC each month based on APCO's estimate of such incremental costs to be incurred during the next month. When such actual incremental costs for that month have been determined by APCO, an adjustment shall be made by APCO to reflect a credit or additional charge to AEC.

4.04 Costs Not Susceptible to Precise Quantification.

(a) In addition to paying its pro rata share of all costs as described in Section 4.01, AEC shall pay APCO a monthly amount equal to ten percent (10%) of the operating and maintenance cost payable pursuant to Section 4.01 to cover costs to APCO which are not susceptible to precise quantification.

(b) In addition to paying its pro rata share of all New Investment as described in Section 4.02, AEC shall pay APCO ten percent (10%) of the monthly charges to AEC associated with such New Investment to cover costs to APCO which are not susceptible to precise quantification.

(c) The amounts provided for herein shall be reflected on the bills rendered in accordance with Article V relating to estimated costs and shall be due and payable as of the time specified therein. Such amounts shall be adjusted at the times actual expenditures have been determined.

ARTICLE V

Billing

5.01 Billing Methods. Billing for all payments due under this Operating Agreement shall be in the format provided in Appendix C.

5.02 Rendering Bill. APCO shall render to AEC monthly a billing statement no later than the twentieth (20th) day of each month, transmitted by wire or delivered by courier, covering the estimated amounts due for the next succeeding month for (a) operating costs pursuant to Section 4.01; (b) New Investment costs pursuant to Section 4.02; (c) incremental costs pursuant to Section 4.03; and (d) costs specified in Section 4.04. When the actual expenditures for operating costs, New Investment costs and incremental costs for that month have been determined by APCO and recorded on its books of account, an adjustment shall be made by APCO to reflect a credit or additional charge to AEC and such credit or additional charge shall appear, with interest at the Regular Interest Rate payable to the appropriate party, on the monthly invoice next delivered after determination of the actual

expenditures. A credit or additional charge shall also be made because of the impact which any such adjustment to actual cost would have on charges under Section 4.04.

5.03 Payment. Payment for items billed under Section 5.02 shall be due on the first day of the month following the month in which the bill is presented. The obligation to make payments as specified herein shall continue notwithstanding the capability (or lack of capability) of the Farley Plant to produce power, for any reason. If payment is not received by such due date, interest at the Special Interest Rate will accrue from date due until payment is received. In the event payment is made in an amount less than the amount due pursuant to the bill rendered, the monies paid to APCO by AEC shall be applied, first, to any interest due to APCO under the Basic Agreements; second, to incremental costs pursuant to Section 4.03; third, to AEC's share of operating and maintenance expenses of the Facilities pursuant to Section 4.01 and other costs specified in Section 4.04(a); and fourth, to New Investment costs pursuant to Section 4.02 and other costs specified in Section 4.04(b).

5.04 Methods of Payment. All payments required to be made by AEC under this Operating Agreement in excess of $10,000 shall be paid on or before the due date in immediately available funds by delivery (before 11:00 a.m., Birmingham time) of either a Federal Reserve check or evidence of bank wire to APCO's account, at a bank designated by APCO. If any

such payment is to be made by bank wire, APCO shall advise AEC of the appropriate bank and account number at least one business day before the payment is due. All other payments required to be made under this Operating Agreement may be made by check deposited in the United States mail three (3) days prior to the date due, first-class postage prepaid, and addressed to Treasurer, Alabama Power Company, P. O. Box 2641, Birmingham, Alabama, 35291.

5.05 No Arbitration; Resolution of Disputes. Neither party shall have the right to arbitrate any dispute that might arise with respect to this Operating Agreement. Any disagreement between the parties as to their rights or obligations under this Operating Agreement shall first be addressed by consultation between the Authorized APCO Representatives as determined in accordance with Section 19.03 of the Purchase and Ownership Agreement and the Authorized AEC Representative as determined in accordance with Section 19.02 of the Purchase and Ownership Agreement. In the event such representatives are unable to resolve satisfactorily their disagreement, they shall refer the matter to senior management of each party. No dispute as to the payment of an invoice rendered by APCO shall permit AEC to delay payment of the disputed invoice, in full, on its payment date. If AEC shall have paid any such disputed invoice, in full, on or before its payment date and if the Authorized APCO Representative and the Authorized AEC Representative, or the parties' senior management, or a court

of competent jurisdiction, should later determine that a disputed invoice was for an amount in excess of the correct amount due, then APCO shall be obligated to refund the difference to AEC with interest, if any, upon such amount as follows:

(a) If such difference resulted from a deviation from an estimate not caused by error or bad faith, interest shall be payable at the Regular Interest Rate;

(b) If such difference resulted from an error, interest shall be payable at the Regular Interest Rate; and

(c) If such difference resulted from bad faith, such interest shall be payable at the Special Interest Rate.

5.06 Billing Adjustments. Billing errors or adjustments to estimates of $5,000 or more discovered through (i) resolution of billing disagreements pursuant to Section 5.05, (ii) audit, or (iii) normal billing procedures, will be adjusted and interest will accrue at the Regular Interest Rate, unless otherwise determined pursuant to Section 5.05, from the date of payment of the original bill through the date of payment of the adjustment. Adjustments of less than $5,000 will be made, but no interest will accrue.

ARTICLE VI

Accounting Matters and Access to Books and Records

6.01 Responsibility and Method of Accounting. All accounting related to the transactions contemplated by this

Operating Agreement shall utilize the accrual method of accounting and shall be in accordance with Generally Accepted Accounting Principles, FERC's Uniform System of Accounts or as prescribed by other regulatory agencies having jurisdiction all as in effect from time to time.

6.02 Confidentiality. During the term of this Operating Agreement, it may become necessary or desirable, from time to time, for one Party to provide to the other Party information which is either confidential or proprietary. The Party desiring to protect any such information (the labelling Party) may label such information as either confidential or proprietary and thereafter the other Party will not reproduce, copy, use or disclose (except when required by governmental authorities) any such information in whole or in part for any purpose without the written consent of the labelling Party. In disclosing confidential or proprietary information to governmental authorities, the disclosing Party shall cooperate with the labelling Party in minimizing the amount of such information furnished. At the specific request of the labelling Party, the other Party will endeavor to secure the agreement of such governmental authorities to maintain specified portions of such information in confidence.

ARTICLE VII

Management of the Facilities; Liability and Allocation of Risk; and Contracts for the Facilities

The provisions of Article VIII of the Purchase and

Ownership Agreement are incorporated herein by reference and shall apply as if set forth herein in full.

ARTICLE VIII

General Covenants

The provisions of Article IX of the Purchase and Ownership Agreement are incorporated herein by reference and shall apply as if set forth herein in full.

ARTICLE IX

Waiver of Partition

The provisions of Article X of the Purchase and Ownership Agreement are incorporated herein by reference and shall apply as if set forth herein in full.

ARTICLE X

Assignment

The provisions of Article XI of the Purchase and Ownership Agreement are incorporated herein by reference and shall apply as if set forth herein in full.

ARTICLE XI

Insurance

The provisions of Article XII of the Purchase and Ownership Agreement are incorporated herein by reference and shall apply as if set forth herein in full.

ARTICLE XII

Destruction; Condemnation

The provisions of Article XIII of the Purchase and Ownership Agreement are incorporated herein by reference and shall apply as if set forth herein in full.

ARTICLE XIII

Force Majeure

The provisions of Article XIV of the Purchase and Ownership Agreement are incorporated herein by reference and shall apply as if set forth herein in full.

ARTICLE XIV

Default

The provisions of Article XV of the Purchase and Ownership Agreement are incorporated herein by reference and shall apply as if set forth herein in full.

ARTICLE XV

Special Remedies

The provisions of Article XVI of the Purchase and Ownership Agreement are incorporated herein by reference and shall apply as if set forth herein in full.

ARTICLE XVI

Term of Agreement

The provisions of Article XVII of the Purchase and Ownership Agreement are incorporated herein by reference and shall apply as if set forth herein in full.

ARTICLE XVII

Accounting Matters

The provisions of Article XVIII of the Purchase and Ownership Agreement are incorporated herein by reference and shall apply as if set forth herein in full.

ARTICLE XVIII

Consultations and Mutual Cooperation; Authorized Representatives

The provisions of Article XIX of the Purchase and Ownership Agreement are incorporated herein by reference and shall apply as if set forth herein in full.

ARTICLE XIX

Miscellaneous

19.01 The provisions of Article XX of the Purchase and Ownership Agreement are incorporated herein by reference and shall apply as if set forth herein in full.

19.02 Terms used in this Operating Agreement which are defined in the Purchase and Ownership Agreement shall have the same meaning.

IN WITNESS WHEREOF, the parties have hereto caused this Operating Agreement to be signed and sealed as of _____, 1984 by their duly authorized representatives.

ALABAMA POWER COMPANY

ATTEST: By_____

_____
Corporate Secretary

ALABAMA ELECTRIC COOPERATIVE, INC.

By_____

ATTEST:

_____

STATE OF ALABAMA:
to-wit:
JEFFERSON COUNTY

The foregoing instrument was acknowledged before me this ____ day of _____, 1984 by _____ and _____, President and Corporate Secretary, respectively, of Alabama Power Company, an Alabama corporation, on behalf of the Corporation.

My commission expires:_____

_____
Notary Public

STATE OF ALABAMA:
to-wit:
COVINGTON COUNTY

The foregoing instrument was acknowledged before me this _____ day of _____, 1984 by _____ and _____, _____ and _____, respectively, of Alabama Electric Cooperative, Inc., an Alabama corporation, on behalf of the Corporation.

My commission expires:_____

_____
Notary Public

ATTACHMENT 12

NUCLEAR FUEL AGREEMENT

NUCLEAR FUEL AGREEMENT
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NUCLEAR FUEL AGREEMENT

THIS NUCLEAR FUEL AGREEMENT is made and entered into as of the _____ day of _____, 1984, by and between Alabama Power Company (APCO), an Alabama corporation with its principal office at 600 North 18th Street, Birmingham, Alabama, and ALABAMA ELECTRIC COOPERATIVE, INC. (AEC), an electric cooperative organized under Alabama law with its principal office at _____, Andalusia, Alabama:

WITNESSETH

WHEREAS, APCO is an electric utility organized and existing under the laws of the State of Alabama; and

WHEREAS, APCO has constructed and operates a nuclear plant near Dothan, Alabama, referred to as the Joseph M. Farley Nuclear Plant (the "Farley Plant") subject to the requirements of the licenses issued by the Nuclear Regulatory Commission; and

WHEREAS, AEC is a generation and transmission cooperative organized and existing under the laws of the State of Alabama; and

WHEREAS, on August 10, 1981, the Nuclear Regulatory Commission amended APCO's license for the Farley Plant by

requiring APCO to offer to sell to AEC an undivided ownership interest in the Farley Plant; and

WHEREAS, in accordance with the foregoing, APCO has agreed to sell to AEC and AEC has agreed to purchase, on the terms and conditions set forth in the Purchase and Ownership Agreement between AEC and APCO of even date herewith, a 6.26 percent undivided ownership interest in the Farley Plant; and

WHEREAS, the parties recognize that the transactions contemplated hereby were solely the product of administrative and judicial decrees designed to satisfy certain antitrust concerns by providing AEC with access to power generated by the Farley Plant, and that such decrees were not intended to provide AEC with other incidents of joint ownership not explicitly granted herein which might otherwise accompany the sale of such an ownership interest; and

WHEREAS, APCO and AEC, as a part of such arrangement, have agreed on the terms and conditions set forth for the sale to AEC of a 6.26 percent undivided ownership interest in the Nuclear Fuel for the Farley Plant, as well as the basis on which Nuclear Fuel shall be acquired, owned, managed, installed and disposed of in the future;

NOW, THEREFORE, in consideration of the premises and mutual obligations hereinafter stated, the parties hereto agree as follows:

ARTICLE I

Definitions

The words and terms used herein shall have the following meanings and the provisions of Article I of the Purchase and Ownership Agreement are incorporated by reference herein and shall apply as if set forth herein in full except as otherwise defined herein.

1.01 AEC Nuclear Fuel. AEC Nuclear Fuel shall be the AEC Ownership Interest in Nuclear Fuel and shall be calculated as follows: (i) for Designated Nuclear Fuel, a percentage equal to the Percentage Ownership Interest of AEC in each respective Unit for which the Designated Nuclear Fuel is designated, as that percentage is modified from time to time in accordance with Articles XI, XV or XVI hereof and (ii) for Undesignated Nuclear Fuel, the percentage calculated in accordance with the provisions of Section 7.02 hereof, as that percentage is modified from time to time in accordance with Articles XI, XV or XVI hereof.

1.02 Designated Nuclear Fuel. The individual fresh and irradiated nuclear fuel assemblies and associated burnable poison rod assemblies for Farley Units 1 or 2, whether in storage or in use in any such Unit, and any Nuclear Fuel in process, any of which is designated by APCO on its books of

account for use in Farley Units 1 or 2 including, but not limited to, uranium in inventory being converted or enriched and being fabricated or shipped, together with all replacements thereof and additions thereto.

1.03 Facilities. As used herein (and as used in provisions of other of the Basic Agreements incorporated herein by reference), the term "Facilities" shall mean Nuclear Fuel.

1.04 Nuclear Fuel. The Designated Nuclear Fuel and Undesignated Nuclear Fuel (including Spent Nuclear Fuel) described in Exhibit A hereto.

1.05 Nuclear Fuel Contracts. Those contracts for Nuclear Fuel described in Exhibit B hereto.

1.06 Spent Nuclear Fuel. Nuclear Fuel which APCO determines has completed its useful life and which will be stored, transported and reprocessed or disposed of, temporarily or permanently.

1.07 Spent Nuclear Fuel Disposal Costs. Any cost or credit associated with contracts for disposal of Spent Nuclear Fuel.

1.08 Undesignated Nuclear Fuel. All of APCO's uranium inventory and any burnable poison rod assemblies not yet designated by APCO on its books of account for use in any particular nuclear unit, whether acquired for Farley Units 1 or 2 or any other undesignated unit.

1.09 Undesignated Unit. Any nuclear unit owned by APCO, or in which APCO has an ownership interest, other than Farley Units 1 and 2, and any nuclear unit owned by another entity with which APCO has agreed to pool Nuclear Fuel.

ARTICLE II

Purchase of AEC's Percentage Ownership Interest

2.01 Purchase of AEC Nuclear Fuel at the Closing. Subject to the terms and conditions herein set forth, at the Closing, APCO agrees to sell and convey and AEC agrees to purchase and pay for the AEC Nuclear Fuel. Prior to or at the Closing, APCO will secure a release of the AEC Nuclear Fuel from the lien of the Indenture and from any ownership arrangement with Lessors of such fuel to APCO. APCO shall convey title to the AEC Nuclear Fuel by the delivery of a Bill of Sale, substantially in the form of Exhibit C hereto, conveying such undivided ownership interest in all property listed thereon and an Assignment Agreement, substantially in the form of Exhibit D hereto, assigning such undivided ownership interest in APCO's rights, duties and obligations under the Nuclear Fuel Contracts. The parties agree that all assignments under this Section are subject to the provisions of Section 8.03 hereof.

2.02 APCO as Agent of AEC.

(a) AEC hereby reaffirms its appointment of APCO (such appointment to be irrevocable for the term of this Nuclear Fuel Agreement and coupled with an interest) as its sole agent as provided in Section 8.01 of the Purchase and Ownership Agreement, to act on behalf of AEC with respect to all matters specified in such Section 8.01.

(b) As relates to all third parties, this agency designation shall be binding on AEC, and such appointment

shall be deemed in effect by each third party until such third party receives written notification from APCO of any termination thereof.

(c) APCO accepts such appointment. APCO shall have the right to exercise such authority granted to it by AEC through a contractor or agent selected by APCO. In any such event, the authority of such contractor or agent shall be coextensive with the authority granted APCO and such contractor and agent shall be an additional beneficiary of all provisions of this Nuclear Fuel Agreement and the other Basic Agreements including, but not limited to, those relating to responsibility of the party procuring or utilizing the Nuclear Fuel, and payment of cost. APCO's duties and responsibilities under this Nuclear Fuel Agreement shall include, but not be limited to, establishing organizational structure and manpower requirements, designing or arranging for the design of Nuclear Fuel and arranging and procuring necessary or desirable Nuclear Fuel including all materials and services associated therewith. Nothing herein shall interfere with APCO's authority and responsibility for the operation of, maintenance of, modifications to, fueling of, and improvements to all of its other generation facilities.

(d) AEC agrees that it will take all necessary action in a prompt manner to execute any agreements with respect to the procurement of Nuclear Fuel, including any materials or services associated therewith, as and when requested by APCO to permit APCO to carry out its authority and

responsibilities pursuant to this Section 2.02; however, AEC recognizes that it shall be bound by any such agreement entered into by APCO notwithstanding its not having executed such agreement.

(e) AEC expressly agrees that APCO does not, by this Nuclear Fuel Agreement, assume any risks or liabilities to AEC with respect to design, procurement, transportation, handling, management, utilization, or disposal of AEC's Nuclear Fuel and that the amounts paid and payable to APCO under the Basic Agreements are determined on the basis that APCO does not assume any such risks or liabilities.

2.03 Limitation on AEC's Rights as Tenant in Common. The parties recognize that the sale of an ownership interest in the Nuclear Fuel to AEC is the product of administrative and judicial orders designed to satisfy antitrust concerns by providing AEC with an ownership interest in the Nuclear Fuel and not because APCO and AEC mutually determined that it would be in their respective best interests to enter into the arrangement contemplated hereby. Accordingly, APCO and AEC agree that the normal incidents of tenancy in common shall not be applicable to the conveyance of AEC's Percentage Ownership Interest, and that AEC shall have no rights as tenant in common other than those specifically enumerated in the Basic Agreements.

ARTICLE III

Payments for AEC Nuclear Fuel

The provisions of Sections 3.02 through 3.04 of the Purchase and Ownership Agreement are incorporated herein by reference and shall apply as if set forth in full.

3.01 Payment for AEC Nuclear Fuel at the Closing. At the Closing, AEC shall pay to APCO for the AEC Nuclear Fuel being purchased at the Closing the amount resulting from the application of the calculations and subject to the adjustment, both as prescribed in Exhibit E hereto.

3.02 Payments For New AEC Nuclear Fuel. AEC shall be required to make estimated payments for new AEC Nuclear Fuel pursuant to the form of Estimated Expenditures Invoice that is attached hereto as Exhibit F in the same manner, and at the same times, as AEC is required to make payments for New Investment pursuant to Section 4.02 and Article V of the Operating Agreement. Such amounts shall be adjusted at the time actual expenditures have been determined in the same manner as is specified in Section 5.02 of the Operating Agreement, including adjustment for the impact which such actual costs would have on charges under Section 3.03 hereof.

3.03 Incremental Costs. AEC shall be responsible for any incremental costs experienced by APCO associated with the design, procurement, transportation, handling, management, utilization, or disposal of Nuclear Fuel which arises solely as a result of the sale to AEC, or its acquisition, of an ownership interest in the Nuclear Fuel hereunder.

3.04 Costs Not Susceptible to Precise Quantification.

In addition to paying its pro rata share of all costs as described in Section 3.02, AEC shall pay APCO a monthly amount equal to one percent (1%) of the cost payable pursuant to such Section 3.02 to cover costs to APCO associated with Nuclear Fuel procurement for AEC which are not susceptible to precise quantification.

3.05 Adjustment for Westinghouse Settlement. As a result of the litigation between APCO and Westinghouse Electric Corporation ("Westinghouse") over the failure of Westinghouse to furnish uranium associated with Regions 4 and 5 of Farley Unit 1, APCO is entitled to receive future benefits associated with Nuclear Fuel in the form of credits and avoidance of inventory carrying charges. AEC shall be entitled to such benefits to the extent of the ratio of purchases of energy from Farley Unit 1 by AEC Members to total energy of purchases by all of APCO's wholesale and retail customers from such Unit 1 during the period Regions 4 and 5 were in Farley Unit 1. Adjustment shall be made and AEC shall pay APCO for any such benefits it receives because its Percentage Ownership Interest is greater than the ratio described above.

ARTICLE IV

Representations and Warranties

The provisions of Article IV of the Purchase and Ownership Agreement are incorporated herein by reference and shall apply as if set forth herein in full.

ARTICLE V

The Closing and Closing Date

The provisions of Article V of the Purchase and Ownership Agreement are incorporated herein by reference and shall apply as if set forth herein in full.

ARTICLE VI

Conditions to Closing

The provisions of Article VI of the Purchase and Ownership Agreement are incorporated herein by reference and shall apply as if set forth herein in full.

ARTICLE VII

Nuclear Fuel

7.01 Financing of Nuclear Fuel. The parties agree that either party may elect to lease or own its respective ownership interest in Nuclear Fuel. Any such decision to lease or own Nuclear Fuel may be made independently with the result that one party may own its percentage interest in Nuclear Fuel while the other party leases its ownership interest in Nuclear Fuel. Accordingly, the parties retain the right to enter into transactions (whether by lease, heat supply contract or otherwise) for the financing of Nuclear Fuel. The cost of any additional instrumentation required in connection with the financing of Nuclear Fuel shall be the sole responsibility of the party entering into such transaction.

7.02 Undesignated Nuclear Fuel. In the event APCO acquires any other nuclear unit other than Farley Unit 1 or Unit 2, or any interest in any such other unit, or APCO determines that it is in the best interest of APCO to place Nuclear Fuel under a pooling arrangement with nuclear fuel for any other unit, including units owned or operated by others, APCO shall be permitted to do so in its sole discretion. In such event AEC's Percentage Ownership Interest in Undesignated Nuclear Fuel shall be computed in accordance with the following formula:

$$\text{POI UNF} = \frac{\text{PF1} \times \text{POI Unit 1} + \text{PF2} \times \text{POI Unit 2}}{\text{PO} + \text{PF1} + \text{PF2}}$$

where:

P = Thermal power level in Megawatts
F = Appropriate Farley Unit
0 = Other nuclear unit
POI = AEC's percentage ownership interest at that time in specified unit
POI UNF = AEC's percentage ownership interest in undesignated Nuclear Fuel

When any nuclear unit stated in the above formula is permanently removed from service, of if any unit's power level is derated or uprated, the formula as well as the adjustments required by Section 7.04 hereof, will be appropriately adjusted.

7.03 Spent Nuclear Fuel

(a) Subject to the provisions of this Section, AEC will take title to and assume full financial responsibility for its AEC Nuclear Fuel interest in Spent Nuclear Fuel Disposal Costs for all Spent Nuclear Fuel. AEC shall pay APCO

for its portion of such Costs ten (10) days prior to the date APCO must pay such Costs under the disposal contract.

(b) No reduction in the AEC Nuclear Fuel interest pursuant to Articles XI, XV or XVI hereof shall reduce the AEC Nuclear Fuel interest in Nuclear Fuel that is Spent Nuclear Fuel at the time of the adjustment.

(c) As to any future assessment under disposal contracts for the AEC Nuclear Fuel that is Spent Nuclear Fuel as of the Closing Date, the parties agree that AEC will only be responsible for Spent Nuclear Fuel Disposal Costs in excess of that already paid by AEC's Members in wholesale rates in the same proportion as was represented in wholesale rates of such AEC Members. Such amount shall be based on the percentage determined by dividing the total energy purchased by AEC Members from APCO during the period such Spent Fuel was in the reactor by the total energy sold by APCO to all its retail and wholesale customers during such period. For Spent Nuclear Fuel Disposal Costs for Nuclear Fuel that becomes Spent Nuclear Fuel after the Closing Date, the parties will be responsible for a percentage equal to their respective ownership interests in the appropriate Unit.

7.04 Title and Investment Adjustments Whenever Undesignated Nuclear Fuel is Designated.

(a) Any time a batch of Undesignated Nuclear Fuel is designated for a unit other than Farley Unit 1 or Farley Unit 2, APCO shall pay AEC an amount so that the AEC investment (i.e., the amount paid by AEC to APCO for such Nuclear

Fuel, undepreciated, unless otherwise specified in the pooling agreement) in that batch is $0. AEC agrees to execute such title and release documents as are required by Section 16.02 hereof.

(b) Any time a batch of Undesignated Nuclear Fuel is designated for a Farley Unit, AEC shall pay APCO an amount so that the percentage of the total investment (i.e., the amount paid for such Nuclear Fuel, undepreciated, unless otherwise specified in the pooling agreement) of each party in the batch being designated is equal to the respective party's current Percentage Ownership Interest in the Unit for which it is designated. APCO agrees to execute such title and release documents as are required by Section 16.02 hereof.

ARTICLE VIII

Management of the Facilities; Liability and Allocation of Risk; and Contracts for the Facilities

The provisions of Article VIII of the Purchase and Ownership Agreement are incorporated herein by reference and shall apply as if set forth herein in full.

ARTICLE IX

General Covenants

The provisions of Article IX of the Purchase and Ownership Agreement are incorporated herein by reference and shall apply as if set forth herein in full.

ARTICLE X

Waiver of Partition

The provisions of Article X of the Purchase and Ownership Agreement are incorporated herein by reference and shall apply as if set forth herein in full.

ARTICLE XI

Assignment

The provisions of Article XI of the Purchase and Ownership Agreement are incorporated herein by reference and shall apply as if set forth herein in full.

ARTICLE XII

Insurance

The provisions of Article XII of the Purchase and Ownership Agreement are incorporated herein by reference and shall apply as if set forth herein in full.

ARTICLE XIII

Destruction; Condemnation

The provisions of Article XIII of the Purchase and Ownership Agreement are incorporated herein by reference and shall apply as if set forth herein in full.

ARTICLE XIV

Force Majeure

The provisions of Article XIV of the Purchase and Ownership Agreement are incorporated herein by reference and shall apply as if set forth herein in full.

ARTICLE XV

Default

The provisions of Article XV of the Purchase and Ownership Agreement are incorporated herein by reference and shall apply as if set forth herein full.

For purposes of incorporation by reference herein of Article XV of the Purchase and Ownership Agreement, Farley Units 1 and 2 shall include that portion of the Designated Nuclear Fuel used or to be used by that Unit. The AEC Percentage Ownership Interest in the Undesignated Nuclear Fuel shall be adjusted by replacing the 0.0626 in the formula in Section 7.02 hereof with the adjusted AEC Percentage Ownership Interest in each Unit.

ARTICLE XVI

Special Remedies

The provisions of Article XVI of the Purchase and Ownership Agreement are incorporated herein by reference and shall apply as if set forth herein in full.

For purpose of incorporation by reference herein of Article XVI of the Purchase and Ownership Agreement, Farley

Units 1 and 2 shall include that portion of the Designated Nuclear Fuel used or to be used by that Unit.

ARTICLE XVII

Term of Agreement

The provisions of Article XVII of the Purchase and Ownership Agreement are incorporated herein by reference and shall apply as if set forth herein in full.

ARTICLE XVIII

Accounting Matters

The provisions of Article XVIII of the Purchase and Ownership Agreement are incorporated herein by reference and shall apply as if set forth herein in full.

ARTICLE XIX

Consultations and Mutual Cooperation; Authorized Representatives

The provisions of Article XIX of the Purchase and Ownership Agreement are incorporated herein by reference and shall apply as if set forth herein in full.

ARTICLE XX

Miscellaneous

The provisions of Article XX of the Purchase and Ownership Agreement are incorporated herein by reference and shall apply as if set forth herein in full.

IN WITNESS WHEREOF, the parties have hereto caused this Agreement to be signed and sealed as of _____, 1984 by their duly authorized representatives.

ALABAMA POWER COMPANY

By_____

ATTEST:

_____
Corporate Secretary

ALABAMA ELECTRIC COOPERATIVE, INC.

By_____

Attest:

_____

STATE OF ALABAMA:

to-wit:

JEFFERSON COUNTY

The foregoing instrument was acknowledged before me this _____ day of _____, 1984 by _____ and _____, President and Corporate Secretary, respectively, of Alabama Power Company, an Alabama corporation, on behalf of the Corporation.

My commission expires:_____

_____
Notary Public

STATE OF ALABAMA:

to-wit:

COVINGTON COUNTY

The foregoing instrument was acknowledged before me this ___ day of _____, 1984 by _____, of Alabama Electric Cooperative, Inc., an Alabama corporation, on behalf of the Corporation.

My commission expires:_____

_____
Notary Public

EXHIBIT A

[This shall consist of a description of all Nuclear Fuel in which AEC will acquire an interest as of the Closing Date.]

EXHIBIT B

[List of Contracts for Nuclear Fuel cycle elements, e.g., U_3O_8 contracts, conversion contract, etc.]

EXHIBIT C

[Form of Bill of Sale to be Prepared.]

EXHIBIT D

[Agreement to assign pro rata share of rights, duties and obligations under Nuclear Fuel Contract.]

EXHIBIT E

[PRICE - TO BE NEGOTIATED]

EXHIBIT F

[Form of Invoice for AEC's share of estimated Nuclear Fuel expenditures for fuel in the future.]

AFFIDAVIT OF CHARLES J. CICCHETTI

I. Introductory

1. My name is Charles J. Cicchetti. My business address is 315 W. Gorham St., Madison, Wisconsin. I am Vice President of National Economic Research Associates and Senior Vice President of Madison Consulting Group, Inc.

2. I received my B.A. in economics from The Colorado College in 1965 and my Ph.D. in economics from Rutgers University in 1969. I performed post-doctoral research in energy and environmental economics from 1969 to 1972 at Resources for the Future (RFF) in Washington, D.C. In 1972, I joined the faculty in economics and environmental studies at the University of Wisconsin, Madison. Since 1978, I have been a Full Professor at that University. My teaching and research has been in the areas of applied economics, energy and regulatory policy.

3. In 1975 and 1976, I was director of the Wisconsin Energy Office and the member of Governor Patrick Lucey's Cabinet who was responsible for developing the state's near- and long-term energy policy. In 1977, I became chairman of the Public Service Commission of Wisconsin, and I served as a commissioner until 1980 at which time I resumed my consulting, teaching and research career.

4. The Public Service Commission of Wisconsin regulates the

pricing, planning and services of the state's public and private utilities. During my tenure we were engaged in determining the economic value, feasibility and pricing of the state's electric utility investments including nuclear generation. My consulting and research activities have been similarly directed at electric utililty generating plant matters.

II. Scope of Assignment

I have been asked to address two subjects:

(1) What is a fair and reasonable price for an ownership share in Plant Farley offered by APCO to AEC pursuant to the NRC License Condition?

(2) What factors should be considered in determining the adjustment to the cost of common equity used in AFUDC calculations, which is discussed at page 14 of Mr. Walker's affidavit?

In preparing this affidavit, I have reviewed the following materials that pertain specifically to this case: (a) The NRC decision imposing licensing conditions on Alabama Power Company (APCO), (b) Written communications between APCO and Alabama Electric Cooperatives (AEC) regarding the sale of a portion of the Farley Nuclear plant, and (c) Other filings and affidavits filed in this proceeding.

III. Fair and Reasonable Price

A. Context of the Sale

I understand that APCO has been required to offer to sell to AEC an ownership interest in Plant Farley because the NRC's Atomic Safety and Licensing Appeal Board ("ALAB") found that, in

the absence of license conditions, activities under the licenses for Plant Farley would create or maintain a situation inconsistent with the antitrust laws. Based on my reading of the ALAB's decision and on the advice of counsel, I understand that the objective of the conditions imposed by the NRC is to provide an opportunity for increased competition in the future, not to punish APCO or reward reparations to AEC for any past injuries. Accordingly, this part of my inquiry focuses upon the following question: What is a fair and reasonable price for a sale required by an antitrust tribunal with the objective of increasing opportunities for competition in a market?

B. Standard for Fair and Reasonable Price

In my opinion, fair market value is the appropriate measure of price to be applied in this case. This is the same standard used by courts considering the terms of divestiture decrees, and is consistent with essential facility doctrine. Under this standard, the price paid should be no less than that which would prevail in a competitive market. A price calculated on any other basis would penalize APCO and its customers, contrary to the purpose of the ALAB's order and in conflict with the proposition that the remedy is intended to create future opportunities for competition rather than award, and assess, damages for past conduct.

Permitting APCO to recover the fair market value of the interest sold would permit it to derive any economic incentive rents that it has earned by superior performance in constructing and operating Plant Farley, a result that furthers antitrust and

economic efficiency policies. It is also a result that is consistent with the principle that has been applied in other contexts in which sale of an asset may be required under the antitrust laws.

1. Economic Incentive Rents: To an economist, fair market value has no precise definition. It depends upon the specific circumstances of the matter under consideration. The floor, or low value, associated with the term fair market value is usually associated with the price that would be expected in a perfectly competitive market. That floor would be determined by calculating the cost of service or supply. It would include a fair return on the invested capital, including full compensation for risks undertaken by the owner prior to sale.

This floor does not take into account the existence of characteristics, including possession of a rich source of raw materials, a desirable location, or significant, not-readily-replicated, productive, marketing and entrepreneurial advantages. Any one of these may result in firms which possess such characteristics earning greater returns than the perfectly competitive market norm. This above-normal return would be included in the definition of economic value and it would normally be reflected in a determination of fair market value. In fact, such additional returns should be encouraged and condoned by society in a market-driven economy. This would encourage economic efficiency due to the fact that firms finding and developing rich resources and superior locations, as well as achieving superior production and

performance techniques, should be encouraged through higher than normal market returns.

Economists call such returns "scarcity rents." I prefer a more precise term, namely "economic incentive rents." The principles apply with even greater force when the asset in issue is a nuclear power plant. It is ironic that, in the years since Congress made the "practical value" finding on which the 1970 amendments to the Atomic Energy Act were based, commercial nuclear power has been identified as an extremely risky venture for an electric utility. This perception of risk is the principal reason why no new applications have been submitted to the commission in recent years. Where a licensee has succeeded in this environment, substantially because of the skill and care that it has applied to development of Plant Farley, to deprive it of the fruits of its superior performance would be contrary to sound public policy and certainly to the policies that underlie the antitrust laws.

The concept of "economic incentive rents" is directly relevant to the matter of APCO's sale to AEC of a portion of Plant Farley. The plant is clearly above average in terms of its economic and operating performance. (I will discuss this matter below.) The owner of such a plant should therefore expect a sales price for a portion thereof which is above the typical floor price.

For nuclear power plants the distinctions that I am describing with respect to market value have much more than theoretical significance. Consider the stockholders, or retail ratepayers, of a utility, such as Consumers Power Company, that owns a nuclear

plant with significant cost over-runs, and which most likely will never be completed. Competitors of that utility, given the opportunity today to buy a portion of this plant, would pay very little, if anything, for such a plant.

In such a circumstance, fair market value would be below cost plus a normal return. Similarly, when the opposite occurs and a power plant is a superior one, then its owners and retail customers should receive an above-normal return if they are required to sell their plant. The reason is simple: the value of such a plant exceeds the floor market value. It is clear in this case (I will explain why below), that any value to APCO that Plant Farley has over its original cost results in large part from skill, foresight and efficiency. Using the principle of economic efficiency and the concept of fair market value, APCO should be entitled to the "economic incentive rents" associated with its superior performance.

2.Analogy to Divestiture and Essential Facility Situations: In a number of respects, divestiture cases decided under the antitrust laws appear to be analogous to the case at hand. The objective of divestiture is to remove threatened impediments to competition by reducing the concentration in ownership of production facilities. Because the purpose of the remedy is to prevent future abuses of market power, rather than to penalize the divesting firm, the courts generally endorse the fair market value standard. In the context in which there are a significant number of competitors, courts and agencies usually do not need to address specifically

the issue of determining "fair market value." The market mechanism sets the "fair market value," and it is most often relied upon in such circumstances to set the sales price of the divested asset.

Recovery of fair market value for divested assets promotes the economic efficiency objectives described above. This is because the assets retain their "scarcity" or "economic incentive" value, since competitors will bid for access to the "superior" asset. Gains associated with superior good fortune or skill would, therefore, continue to be part of the future income stream generated by the divested assets. Potential buyers, even if numerous, would compensate the owner of the divested asset for its above-normal return. Economists call the basis of the sale of an asset its "opportunity cost" when the sales price is based upon what it would be worth if the seller had retained it.

When a single specified purchaser is permitted to acquire an asset, courts and agencies should strive to reflect in their administrative determination of "fair market value" the same factors that would be relevant if the market actually determined the value. Put more succinctly, fair market value is established by contrasting the willingness of buyers to pay with the willingness of sellers to sell, both of which are based upon the asset's expected stream of future value.

Except in distress situations, which is certainly not the case with respect to Plant Farley, or a situation in which a utility must sell to alleviate acute financial problems, a willing seller would expect and demand to recover its full cost of supply

including the actual expected return on the investment. This is equivalent to its replacement value, i.e., opportunity cost. In divestiture cases, expected return would include any additional returns due to superior skill, efficiency and good fortune.

Plant Farley does not appear to be an essential facility in the sense that access to it is essential to the competitive viability of any firm in the electric power business in Alabama. However, the policies furthered by the fair market value standard also apply when a firm is required to grant access to an essential facility. These cases suggest that the owner of a facility not practically duplicable by competitors has an obligation, if feasible, to share access with competitors on fair and reasonable terms. See A.D. Neale, The Anti-trust Laws of the United States, (1970) at 66-70; pages 66-70, supra, Note 4-, at 67, Second Edition 1970, Sullivan, Handbook of the Law of Antitrust, 148 (1977) at 131. The purpose of this access remedy is to create additional competitive opportunities rather than to punish the essential facility owner. Therefore, applying the essential facility doctrine does not preclude the owner of the essential facility from charging its full economic value.

Access on fair, reasonable, and nondiscriminatory terms does not suggest that anything but full asset value should be reflected in the price. This means prices should reflect the full cost of supply, including "scarcity rents" ("economic incentive rents"). The conclusion that a facility is essential does not affect the

return that should be reflected in any sale, which is associated with any specific fortunate and advantageous circumstances achieved by owners of the essential facility at their own cost and for which they bore the complete array of associated risks. If anything, antitrust policies, and economic efficiency, favor the creation of incentives for the development of essential facilities, and would be undermined if owners were required to accept less than fair market value when ordered to grant access to competitors. Thus Sullivan is correct in concluding that the essential facility law should not "be extended to compel prices which yielded no more than competitive [i.e., cost plus returns at the normal rate] returns." Sullivan, Handbook of Antitrust Law, 48 (1977) at 127.

The fact that APCO is a regulated public utility does not alter any of the conclusions that I have reached. The retail customers of a public utility, who are denied the continued full use of the facility through divestiture, are probably significantly adversely affected. Forced divestiture will transfer to others some of the advantages that they as public utility customers could expect to receive over the asset's life. This transfer represents an opportunity cost, which means that replacement capacity of a comparable economic character will have to be found sooner than otherwise. Such replacement capacity must either be purchased in the open market, or provided through construction of new capacity which is not likely to compare favorably with Plant Farley.

Accordingly, even if the essential facility doctrine applies, AEC should pay APCO a fair market value, which reflects "economic incentive" or "scarcity" return as well as normal returns.

C. Determination of Fair Market Value

In the previous section, I concluded that APCO is entitled to receive the fair market value for the share of Plant Farley sold to AEC pursuant to the Appeal Board's order. This standard requires the prevailing price to equal that which would be paid by willing buyers and accepted by a willing seller in a commercial transaction. No rational seller in such circumstances would agree to forego receiving its opportunity cost, which, if it has a long term need for the production capacity, is not less than the cost of replacing the capacity sold. In my opinion, because taking a portion of Farley off APCO's system accelerates the time at which that portion must be replaced for the other customers of APCO, AEC should, at minimum, be required to pay a price based upon the opportunity, or replacement cost of the plant.

In APCO's initial sales offer to AEC, the price was derived by averaging APCO's estimated total costs associated with Plant Farley, and a value yielded in a study by EBASCO Services, Inc. of the cost of replacing Plant Farley with a similarly sized nuclear plant expected to commence operation in July, 1983.

It is my opinion that the EBASCO figure of $1,724/kW underestimates the replacement cost of Plant Farley. The EBASCO study assumed facts that are overly conservative, including assumptions that all regulatory requirements, economic and political

considerations were known at the commencement of the design phase. The EBASCO study further assumed that these factors remained constant during the lengthy engineering and construction process, and, therefore, that changes in these factors did not affect project costs. In reality, the changes in these factors have significant cost consequences. The result is that the actual replacement value of Plant Farley is significantly higher than EBASCO's calculation.

This is apparent when the replacement cost estimated by EBASCO is compared with the current cost estimates of several nuclear power plants, construction of which actually began contemporaneously with Plant Farley. Comparing costs per kW for nuclear plants is difficult, but not impossible. It is not, as some maintain, like comparing "apples and oranges," but it is not quite as simple as comparing an apple in your left hand with one your right hand. For example, one has: (a) to adjust for constant versus nominal dollars; (2) to decide whether to include AFUDC, or not; (3) to distinguish between the first plant built at a site and subsequent add-on units at the same site; etc. In Attachment 6 to Mr. Franklin's affidavit, data is presented for nuclear units that have either recently been, or are projected to be in the near term, completed plants. This data reflects cost, in constant dollars, exclusive of AFUDC.

EBASCO's estimated replacement cost of Plant Farley is shown to rank between the 6th and 7th of the 31 currently-near-to-completion-date nuclear plants included in Mr. Franklin's analysis.

One of those plants, Marble Hill 1, has been canceled. Another, Diablo Canyon 1, has been beset with extraordinary political opposition and attendant delays.

My conclusion is that if APCO could replace Plant Farley at the cost per kW estimated by EBASCO, it would be fortunate and prudent to do so. I do not think that it can, however. Let me explain why. Compared with the costs projected by utilities now constructing nuclear plants for completion of those units, APCO's offering price, which is lower than the conservative EBASCO study's estimate of replacement cost, is especially attractive. The decision of these utilities nevertheless to continue construction is a significant indicator that the higher costs projected by them represent a significant measure of both the fair market value and the replacement cost of nuclear generating capacity. I conclude, therefore, that APCO's offering price is well below the fair market value.

D. Total Original Cost

I have also been asked to give my opinion as to certain factors that should be taken into account in determining APCO's total original cost associated with Plant Farley. An accurate economic determination of original costs should contain return on common equity ("ROE") that compensates the common stockholder for the risk associated with APCO's investment in Plant Farley. It is clear that the ROEs used to record AFUDC during construction of Plant Farley do not do this. My opinion is based on several

considerations. Before explaining these, let me digress to explain the relationship between risks and return.

To understand the difference between "risk" and "return" consider two alternative investments: (1) purchase security A with an expected return of 10%, and a variance of plus or minus 0% (i.e., security A is a riskless investment); and (2) purchase security B with an expected return of 12%, and a variance of plus or minus 3% (i.e., security B is a "risky" investment).[1]

Quite obviously, if the variance, or risk, associated with security B was zero, no investor would purchase security A over B because B has a higher expected return than A. It is also obvious that if security B retained its variance, i.e., risk, and was also expected to have the same return as the riskless security A, no investor would purchase security B.

A rational investor could even be indifferent between a riskless security and one with a higher expected return, but with some risk, i.e., variance around its expected value. Consider the case in which a typical investor was indifferent between a security with a certain 10% return and another security with a most likely (in a probability sense) expected return of 12%. Furthermore, the reason for this indifference was that there was a significant positive probability (i.e., a non-zero variance) that the actual

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[1]Note: More precisely, variance is always positive. However, its square root, or return on the assets' standard deviation, is a plus or minus concept. I have used the plus or minus concept in the text to avoid introducing additional mathematical complexity, while at the same time making the important point that expected returns for risky assets can both be exceeded and missed.

return on the risky investment will fall below the 10% riskless rate. When there is an indifference between a riskless security and the risky security as described in this example, the differential in expected returns at the point of indifference is called a "risk premium."

I shall now enumerate the reasons why accounting costs, adjusted to reflect the concepts discussed in Mr. Walker's affidavit, do not represent the true cost of Plant Farley, when the risks undertaken by APCO are included in the analysis. First, as Mr. Franklin has testified, the common stock of the Southern Company, APCO's parent, traded substantially below book value during most of the time when Plant Farley was under construction. A market price equal to book value is an important criterion for establishing the financial integrity of an electric utility. When stock trades below book value, each new share that is issued to finance construction produces a dilution in the book value of the investments of existing shareholders. This is a real dollar loss to existing stockholders.

On a company-wide basis, while Plant Farley was under construction and during its early years of operation, APCO did not earn ROEs sufficient to compensate its shareholders fairly. When this happens, it probably means that regulators are not permitting electric rates to increase to sufficient levels to cover the cost of attracting and servicing the capital necessary for construction of new facilities. Rational investors would accept this dilution if they expect to recoup the associated losses in the future over

the life of the facility being constructed. When "willing sellers" sell a portion of the investments financed by dilution, investments in facilities that have been completed successfully in the face of substantial risk, stockholders expect and deserve to be made whole through the sales price for losses suffered during construction and early years of operation.

Second, even if regulators had allowed APCO to earn ROEs adequate to compensate APCO's stockholders for the risks associated with the enterprise as a whole, which they obviously were not, there is higher incremental risk associated with construction of a nuclear plant. Accordingly, APCO should receive a risk premium in the sales price of Plant Farley to adjust for the higher variance, or risk, associated with its investment in Plant Farley, as contrasted to APCO's average embedded investments. Public utility accounting treats an electric utility's activities on a composite basis, since rates are determined by allocating total company costs among various classes of ratepayers. However, if one is attempting to assess the actual cost of a particular activity, the appropriate measure of required return, or cost of capital, should not be based upon the risk of the enterprise as a whole, but upon the incremental risk associated with the construction project.

A study recently completed for the Department of Energy concludes that the estimated risk premium for electric utilities with nuclear plants contrasted with non-nuclear plants is about

"1 to 2 percentage points."[2] If a nuclear project increases a utility's cost of common equity capital by 1% to 2% on a total basis, the incremental cost of common equity capital for a segregated nuclear project must be several percentage points higher than the ROE that is compensatory for the company as a whole.

Third, in retrospect, the actual experience of utilities that commenced nuclear generating projects at the same time that APCO commenced Plant Farley confirm that APCO took the very substantial risk of losing all, or a large part, of its investment in Plant Farley. This was undoubtedly a much greater risk than was perceived at the time. To understand this fact, one only has to consider that the same DOE study referenced above indicates that:

> As of the end of 1982, 42 nuclear plants with more than $50 million in investment expenditures each had been canceled. The total abandonment costs of all nuclear cancellations were about $10 billion. The Nuclear Regulatory Commission (NRC) and industry experts have also indentified a number of other projects which could be canceled. If all of these "at risk" plants were canceled today, approximately another $8 billion of abandonment costs could be incurred.
>
> ...typically, the ratepayers and share-holders each bore about 30 percent of the abandonment costs. The remaining 40 percent of the costs was allocated to society through reductions in the utility's tax liability.[3]

It is clear that the ROEs allowed APCO, on a company-wide basis, by regulators during construction of Plant Farley, do not adequately reflect the risks APCO bore in bringing Plant Farley

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[2]"Investor Perceptions of Nuclear Power," DOE/EIA-0446, Washington, D.C.: Energy Information Administration, May 1984, page 43.
[3]Id. at 7.

from the drawing board to its current status as a plant with a proven record of superior operation. Quantification of this risk requires judgment; there is no purely objective method available. Two additional considerations should be taken into account. These deal with first a retroactive consideration of the relation between risk and return. In addition, I will expand on the notion that I have mentioned several times above that Plant Farley compared to other nuclear plants built under similar conditions, principally in the era following the D.C. Circuit's Calvert Cliffs decision, is an extraordinarily superior nuclear plant.

I will address the additional conceptual matter first. In the previous discussion of risk and expected return, I compared two investments: one was riskless; and the other had a higher expected return accompanied by some uncertainty associated with the variance around the expected return. I explained that a priori rational investors might be indifferent between these two choices. Suppose the more risky choice had been selected; and furthermore, the investor was in a particular circumstance rewarded with a truly favorable outcome in that the actual return earned exceeded the riskless rate plus the risk premium that a priori had made that investor essentially indifferent between the two choices (i.e., the riskless investment versus the higher expected return with higher variance investment). In this favorable case, retrospectively the investor's return would even exceed the risk premium adjusted return.

If the investor sold this investment after it was known that the outcome was more favorable than even the risk-adjusted expected return, the investor would be paid a price which reflected this information. In other words, the investor would be paid for giving up the opportunity to continue to gain the benefits associated with earning these higher than even risk premium adjusted returns.

I will now turn to a fact that I have previously noted concerning Plant Farley. Recently my colleagues at National Economic Research Associates compiled a data base of operating and under construction nuclear plants. In analyzing that data, I find that Plant Farley compared to other post-Calvert Cliff nuclear plants is superior in two important ways relative to other nuclear plants. These are: (1) the cost per kW of installed capacity; and (2) the unit's capacity factor. The construction costs of Plant Farley are nearly 20% below the amount that would be predicted for a plant with its characteristics. Furthermore, in two out of every three years of its operation, the actual capacity factor of Plant Farley is at or above the amount that would have been predicted for it. Mr. Franklin's affidavit offers additional explanation concerning the excellent capacity factor performance of Plant Farley. He also describes some very reasonable explanations as to why Plant Farley was unavailable during various periods and why modifications made during these outages are expected to enhance the future performance of the plant.

Based upon this analysis, I have no doubt that both: (a) the fair market value or replacement cost of Farley is above the EBASCO

estimate; and (b) the return that is due the stockholders and ratepayers of APCO significantly exceeds the cost of common equity capital that is used in APCO's recorded AFUDC rates.

UNITED STATES OF AMERICA

BEFORE THE

NUCLEAR REGULATORY COMMISSION

STATE OF ALABAMA)

JEFFERSON COUNTY)

CHARLES J. CICCHETTI, being first duly sworn, deposes and says that he has read the Affidavit of Charles J. Cicchetti and that the matters and things set forth therein are true and correct to the best of his knowledge, information and belief.

Charles J. Cicchetti

Subscribed and sworn to before me
this the 3rd day of October, 1984.

Jo Ellen G. Kilson
Notary Public

My Commission Expires: 5/30/87

Affidavit of Philip C. Kron

My name is Philip C. Kron. I am a Vice President, Senior Credit Officer and Senior Professional at Citibank, N.A. I have been Department Head of Citibank's Energy East Department since January 1, 1979 and in that capacity supervise the bank's relationships with Eastern-based electric and gas utilities as well as certain diversified energy companies. Citibank is a major lender to the electric utility industry and the customers served by my Department include virtually all of the large electric utilities in the Eastern half of the United States. Total commitments to the industry aggregate several billion dollars.

I graduated from Dartmouth College with an AB degree in 1960 and graduated from the Amos Tuck School of Business Administration at Dartmouth College in 1961 with an MBA. After spending three years on active duty as an officer in the U.S. Army, I spent four years with Price Waterhouse; two years in auditing and two years consulting. I am a CPA in the State of New York. I joined Citibank in late 1968 and have been employed there for the past sixteen years. I have spent approximately seven years lending to the electronics industry, two years in our corporate work-out area handling bankruptcies, a year handling financially ailing real estate companies and six years managing utility relationships.

During my experience over the past six years with utilities, I have become deeply involved with the risks, problems and issues related to nuclear power. I have been actively involved with GPU in the aftermath of the accident at Three Mile Island as Citibank was agent on the $400 million bank credit which provided the company the financial flexibility to avoid bankruptcy after the accident. This role required providing testimony to the state public utility commissions in both New Jersey and Pennsylvania and to committees of both Houses of the U.S. Congress. I have also been intimately involved with the nuclear-related financial problems of Public Service Company of New Hampshire and Long Island Light Company.

My experience with GPU and the accident at Three Mile Island would appear to have direct relevance to Alabama Power Company's ("APC") concern about the capacity and motivation of Alabama Electric Cooperative's ("AEC") in that it relates to contingent costs relative to the operation of a nuclear power plant. As a result of the accident, GPU has incurred well in excess of $1 billion in uninsured and unrecoverable costs. This was an accident that occured over five years ago and, while another accident is remote beause of safety-related improvements accomplished in the industry since then, the costs could be much higher.

A second type of contingent cost which may occur as a result of operating a nuclear plant is referred to as decommissioning costs. These are the costs which will be involved after the useful life of a nuclear plant ends and which will be required to deal with the residual radioactive decontamination. The nuclear power industry has had little, if any, experience with these costs to date given the newness of nuclear power and there is a lot of uncertainty about what will be required and how much it will cost. However, these costs do represent a potential claim against the owner of a nuclear plant which could be large and which would come at time when no current benefit in terms of the generation of electricity is being derived from the plant.

If the contingent costs referred to above ever became real costs relative to the Farley Nuclear Plants and were material in amount, then a decision might be appropriate regarding whether to try to absorb such costs or to avoid them. One possible way of avoiding the cost would to be to file for protection under the bankruptcy laws. But, a bankruptcy proceeding normally involves a large loss to the equity investors of the enterprise and, therefore, a decision to opt for bankruptcy often is affected by how much the equity investors stand to lose. If the equity investment is large, then the loss potential in a bankruptcy proceeding is also large and, therefore, opting for a proceeding may be unattractive. On the other hand, if the equity investment is small, the loss

potential to equity investors in a proceeding would be low and, thus, bankruptcy might be an at' ctive alternative.

I have reviewed the financial statements of APC which reflect that it has an equity investment in excess of $1.5 billion standing behind the performance of its obligations. I have also reviewed the financial statements which reflect AEC's financial position at the end of 1982 and the end of 1983. These were reported in the Form 12e filed by AEC with the Rural Electrification Administration (REA). These statements reflect that AEC has liabilities in excess of its assets and, at the end of the last two calander years, AEC has had a "negative equity". The property of AEC is subject to a first mortgage lien and secures an indebtedness approximately equal to the net cost of its assets as reflected on its balance sheet. I would conclude, therefore, that AEC equity investors would have little to lose by seeking to avoid material costs by filing for bankruptcy while APC equity investors would have a lot to lose.

As I understand the License Condition requiring APC to offer to sell an ownership interest in the Farley Nuclear Plant, AEC is to bear its pro rata share of the cost of operation and cost of capital improvements to the Farley Plant. It is also a fair interpretation of the License Condition that APC is not supposed to incur increased costs because of AEC's ownership interest. Because the financial condition of AEC does not appear to be as strong that of APC, and because the joint obligations which will be experienced in the operation of a jointly owned plant could be great, it appears reasonable, in my opinion, for APC to take steps to assure itself that AEC will have an incentive to meet all of its financial obligations relative to its ownership in the Farley Plant.

It is my understanding that APC has requested from AEC a variety of forms of security to reduce the risk that it will have to bear AEC's portion of the cost of operation and ownership of the plant. These included: (a) Guarantee by REA;

(b) Second Mortgage on AEC's interest in the Farley Plant; (c) Second Mortgage on AEC's other properties; (d) Guarantee by AEC's member distribution entities; or (e) a fund set aside to assure payment of obligation. In my opinion, it is certainly reasonable and prudent for APC to seek these security devices to protect itself against having to pay costs for which AEC is obligated. It may not be necessary, in order to equalize the risk between the parties, for all of these forms of security to be obtained; however, certainly there needs to be some security provided. In my opinion, the most promising source of security would be a guarantee of AEC's obligations by its owners, i.e., the members of AEC which are the equity investors of AEC. Because of AEC's "negative equity," they have little or no stake in the continued financial viability of AEC. Were AEC to declare bankruptcy, the secured creditors would take over the assets and operate those assets without any substantive impact on the owners. The owners would continue to purchase power from the new operator of the system. Therefore, it only seems appropriate to have the members of AEC in Alabama who have an equity investment in their own systems, ranging from 19.9% to 42.6% as reported by the REA in 1982, to put that equity behind the obligations of AEC.

If AEC is to receive the benefits of an ownership interest in the Farley Plant, it appears equitable that APC, who is giving up such benefits, not be placed in the inequitable position of losing the upside while underwriting the downside.

STATE OF NEW YORK

New York COUNTY

PHILIP C. KRON, being first duly sworn, deposes and says that he has read the Affidavit of Philip C. Kron and that the matters and things set forth therein are true and correct to the best of his knowledge, information and belief.

Philip C. Kron

Subscribed and sworn to before me this, the 5th day of October, 1984.

Notary Public

My Commission Expires: _____

AFFIDAVIT OF RICHARD WALKER

My name is Richard Walker. I live at 1446 Granville Avenue, Park Ridge, Illinois. I am a certified public accountant and Senior Partner in the firm of Arthur Andersen & Co., independent public accountants. My office is at 33 West Monroe Street, Chicago, Illinois.

Arthur Andersen & Co. is an independent public accounting firm with more than 100 offices located throughout the world, of which more than 60 are located in this country. We have among our clientele a large number of companies on the New York Stock Exchange. While we have as clients approximately one third of the electric and gas distribution companies in this country, a substantia. portion of the natural gas transmission companies and independent telephone companies, our clients are for the most part users of utility services rather than suppliers. We are independent public accountants with respect to Alabama Power Company and its parent, the Southern Company.

As a Partner in my firm's Regulated Industries Group, which includes our practice with respect to electric, gas, water and telephone companies, I am involved in my firm's research, development and implementation activities in the areas of utility ratemaking and financing, accounting, Federal income taxes, and management control and decision-making systems. As a CPA, I am qualified to practice before the Internal Revenue Service.

Practically all of my career has been devoted to work on regulated electric, gas and telecommunications companies or on matters related to them. I have performed independent audits of these companies, as a result of which we issued our reports on financial statements. I have designed and installed responsibility and other management control and planning systems, worked on determinations of historical original cost required by state and Federal regulatory agencies and supervised our work in connection with a large number of public financings. I work extensively with company managements and their legal counsel, bankers and other advisors in analyzing and resolving matters related to the size and timing of construction programs, financing techniques, rate regulatory decisions, tax policy, diversification and corporate and capital structures. I am a member of the American Institute of Certified Public Accountants where I have served on various committees and task forces and the Illinois Society of Certified Public Accountants. I am a director of the Iowa State University Regulatory Conference and am a member and past president of the Utility and Telecommunications Securities Club of Chicago which is an association of persons involved in the financial analysis of those companies.

I have testified on rate, financial, tax and other matters before the Alabama Public Service Commission and approximately 30 other state utility commissions, the Federal Energy Regulatory Commission (FERC), the Federal Communications Commission, the Committee on Ways and Means of the U. S. House of Representatives, the Tax Court of the United States, the Joint Committee on Atomic Energy, and the Securities and Exchange Commission.

My testimony has related to such matters as the valuation of rate base (including issues as to the inclusion of construction work in progress, the deduction of reserves for deferred income taxes, the determination of working capital, the use of trended original cost rate base and "economic depreciation", etc.) the propriety of various expense components (including current and deferred income taxes) and the propriety of various depreciation methodologies. I have testified recently on "phasing in" of large investments in electric production facilities into service rates. My testimony before the Joint Committee on Atomic Energy, given in 1974 on a pro bono publico basis at the request of the Staff of the AEC, related to the potential financial impact on electric companies of the Staff's proposal to amend the Price Anderson Insurance Indemnity Act.

I. PURPOSE OF AFFIDAVIT

The License Conditions approved by the Atomic Safety and Licensing Appeal Board provide that Alabama Power Company (APCO) shall offer to sell an undivided interest in Plant Farley Units 1 and 2 at a negotiated price sufficient to fairly reimburse APCO for its proportionate share of its total costs of the units including all costs of construction, installation, ownership and licensing. A "book" cost of Plant Farley is reflected in APCO's records maintained in accordance with the Uniform System of Accounts (USOA) prescribed by the FERC. It must also follow a substantially identical USOA prescribed by the Alabama Public Service Commission (APSC).

The purpose of my affidavit is to set forth, from an accounting point of view, the concepts and considerations as to the adjustments that should be made to the book accounting costs and records to reflect the "total costs", as those costs are not shown by, or are not included in, the basic accounting books and records as they stand. To the extent accounting costs are to be considered in establishing a sales price for Plant Farley, it is my view that the adjustments described herein are essential to properly measure those accounting costs and to achieve a fair and equitable recovery of cost by APCO.

In presenting this Affidavit, I do not imply that all costs would be included, as accounting data do not include current economic or opportunity costs, nor do I address the propriety of costs other than accounting costs which are discussed by other witnesses. Nor do I address other aspects of the sale such as the derivation of the percentage of the plant required to be sold.

II. BASES OF PREPARATION OF APCO'S BOOKS AND RECORDS AND MEANING OF ACCOUNTING DATA

The USOAs define "cost" and other terms and specify with considerable specificity the costs that shall be included in the cost of nuclear plant, such as Plant Farley, and in nuclear fuel. They require that "cost" be the "amount of money paid for property or services" or the cash value equivalent if payment is not made in cash. These costs must be maintained as incurred and not written up for inflation or subsequent sales. The USOAs are thus an "original cost" system requiring cost of property to remain at the level of cost "to the first person devoting it to public service." They also require in General Instruction No. 12 that the cost of each generating unit be maintained separately.

The USOAs also prescribe in detail how depreciation shall be accounted for as an expense for each period and as accumulated in a reserve for depreciation. They also include requirements as to

the handling of retirements, cost of removal and salvage, and property purchased and sold.

The USOAs also provide specific instructions for the classification of all revenues, operating expenses, maintenance, interest and dividends. They also include extensive provisions for accounting for current and deferred income taxes.

The USOAs require the classification of each item of construction cost by work order and property unit. Thus, they produce for a power plant, such as Plant Farley, the asset-specific costs of labor, materials, transportation contract payments, engineering, insurance, etc. Other costs, such as pensions, payroll taxes and administrative and general costs, must be allocated to construction projects on bases that are generally accepted as producing reasonable measures of asset-specific costs.

APCO must, pursuant to the USOAs, include in its construction costs of generating plants the cost of money during the period it is tied up in construction. This cost, referred to as "Allowance for Funds Used During Construction" (AFUDC), is the interest cost of borrowed funds and the cost of preferred and common equity for the period from the time funds are spent on construction until the construction is completed or abandoned.

AFUDC is required by the USOAs to be computed by a formula which does not produce an asset-specific cost. It uses overall, rather than specific incremental cost; and it uses historical, embedded rates for debt and preferred stock money rather than the

cost rates of securities actually issued during the construction period to finance the specific construction. Thus, for example, if at the end of 1980, a company had two series of bonds outstanding -- a $1,000,000 series issued in 1955 at an interest rate of 5% and a $1,000,000 series issued in 1979 at a rate of 15% -- the cost of debt used in the AFUDC formula would be based on the weighted average of the two series, or 10%. Obviously, this understates the cost of money that was borrowed in 1979 to finance asset-specific construction expenditures made in 1979.

III. DETERMINATION OF APPROPRIATE ACCOUNTING DATA IF USED AS A COMPONENT OF PLANT SALES PRICE

The public utility accounting system is used to provide data that is useful to regulators who determine the utility's rates. Therefore, one must be careful not to interpret accounting data out of context. Two examples are particularly pertinent here.

First, utility rates are ordinarily fixed by allocating to each class of customers responsibility for a certain percentage of all of the utility's generating capacity. Rate regulators do not ordinarily disaggregate a utility's power supply system for ratemaking purposes. Therefore, the utility accounting system is designed to provide aggregate, rather than asset-specific, data, and the cost figures shown on a utility's books as being attributable to a particular generating plant must be adjusted if one's objective is to determine the real costs attributable to a particular generating facility.

Second, as applied over the entire life of a generating facility, the utility accounting system operates to permit a utility to recover from its customers all of its tax expenses so as to derive, on an "after-tax" basis, the rate of return allowed by the regulatory process, including recovery, after taxes, of all AFUDC. This principle has been recognized since the Galveston case was decided in 1912. Rate regulators have also developed complex procedures for allocating the benefits of tax deferrals between generations of customers.

When a plant is sold, the continuity of the accounting provisions prescribed by ratemakers is broken. It is necessary to make provisions in the sale price for income taxes if APCO is to receive a full return of its investment as well as the return on capital devoted to construction to which it is entitled. In particular, income taxes related to recovery of AFUDC must be included in the sales price if investors are to receive the return on capital which is attributed to the construction period.

Any shortfall in recovery of capital investment or return on investment during construction would fall either on APCO customers or investors. The effect of any shortfall can also be expected to increase capital costs to APCO's remaining customers.

The specific allocations and adjustments of aggregated book costs necessary to find accounting costs that are relevant and useful to setting a price for a sale of Plant Farley are set forth below.

ITEM 1: Restore "Deferred Taxes" Which Were Used to Reduce Recorded AFUDC Cost But Which Must be Repaid in Event of Sale

This is an adjustment to recorded book costs which is necessary for APCO to recover its debt interest cost attributed to Plant Farley while it was being constructed. As stated previously, the USOAs prescribed by the FERC and the APSC provide that the construction cost shall include an "Allowance for Funds Used During Construction" computed in accordance with a specific formula.

The specific formula provides for the computation of the AFUDC rate -- a rate which is applied to the construction cost balance each month, including AFUDC capitalized in prior years -- to arrive at the AFUDC to be capitalized in the accounts for the month. The USOA formula provides that short-term borrowings shall be attributed first to construction; the balance of construction is then assumed to be financed in proportion to the capital structure -- the long-term debt, preferred stock and common equity as shown by the book of accounts at the end of the prior year.(1)

(1) The AFUDC procedure is necessary in a regulated environment as the rate of return allowed after the property is placed in service is limited to the estimated cost of capital at that time. By capitalizing AFUDC, investors are permitted to "earn" a return (at the AFUDC rate) during the period of construction as they will not be permitted to make up the shortfall by higher earnings after the property is in service. The AFUDC capitalized is depreciated annually together with the other plant costs, thus providing a basis for investors to recover this capital cost arising during the construction period.

The USOA formula for AFUDC may be applied by using either of two alternative methods for the handling of the income tax effects of interest cost which is deducted currently for income tax purposes even though capitalized in the accounts as part of AFUDC. This is a "timing difference" and creates "deferred income taxes". These two AFUDC methods, described below, are referred to as the "net-of-tax" method and the "gross" method. The "net-of-tax" method is used by APCO.

At the time the construction interest is deducted for income tax purposes, income taxes payable are reduced, and an equal and offsetting provision for deferred taxes may be made. For ratemaking purposes, regulators have determined that customers should be given the benefit of the interest-free capital that is associated with tax deferrals. The alternative procedures have been developed to accomplish this objective. If this provision for deferred taxes is credited to the construction accounts (as a reduction to the interest components of AFUDC) the utility is said to use the "net-of-tax" AFUDC method. If, instead, the provision for deferred taxes is credited to a separate credit or "reserve" account, "Accumulated Deferred Income Taxes", the interest component of AFUDC capitalized is not reduced and the utility is said to use

the "gross" method. The two methods are equal as the "net-of-tax" method is as though the reserve for deferred taxes were simply a credit account among the debit plant accounts. By reducing rate base by either of the two methods, the benefit of interest free loans from the U.S. Government are passed along to customers.

The income tax effects of the interest timing difference (the deferred taxes) is not a reduction in the original construction cost of the plant. Rather, it is the same as interest-free loans from the U.S. and the State of Alabama which have to be repaid in an amount computed at tax rates in effect at the time, either on the sale of the plant, or as depreciated over its service life if not sold. The sale of a portion of Plant Farley triggers the repayment of a proportionate part of these interest free loans. As they must be repaid, they are not available as a credit to reduce the cost of Plant Farley and, accordingly, must be restored if investors are to be reimbursed for the cost of their investment not yet recovered through depreciation.

Thus, deferred taxes do not increase (or decrease) the cost of plant, but must be identified separately in order to show correctly the actual cost of the plant. It would be unfair to deny APCO the opportunity to recover its actual undepreciated cost of constructing Plant Farley, and illogical to do so in reliance on an accounting convention that has nothing whatsoever to do with the actual cost of constructing Plant Farley. The adjustment that I have described must be made in order to prevent an out-of-pocket loss to APCO.

ITEM 2: Income Taxes Necessary to Recover Preferred Stock and Common Equity Portions of AFUDC

As stated previously, the USOAs require the capitalization of capital carrying costs during construction (AFUDC). These costs include the embedded (historical) rate of preferred stock and the rate on common equity last granted by rate regulators in the primary jurisdiction (Alabama).

The cost rates for preferred stock and common equity used in AFUDC computations, and in utility rate regulations generally, are after-tax rates. Thus, illustratively, to realize a 15% after-tax rate on common equity, an additional 15% must be provided to take care of income taxes, at a 50% tax rate. This procedure is widely recognized in utility regulation, accounting and finance. The factor used to expand the after-tax amount into a pre-tax amount is often referred to as an "expansion factor".

For equity investors in Plant Farley to remain whole, by recovering these after-tax components of AFUDC, utility rates must, and under standard ratemaking procedures do, include each year the related income tax. If that tax component is not received, investors would be deprived of the recovery of their costs as established under the regulatory procedures of the FERC and the Alabama Commission.

The same is true if a sale takes place. The income tax cost on the capitalized equity costs is immediately incurred rather than being distributed over the remaining property life. Thus, the

sale price must include both the preferred and common equity components and also the related income tax (computed at a current expansion factor of 1.90448, based on a rate of 46% Federal and a state rate of 5%, for a combined rate of 47.4923%).

ITEM 3: Determine Actual Cost of AFUDC Incurred to Construct Plant Farley

Ordinarily, the FERC's formula for AFUDC, which uses historical embedded rates for debt and preferred stock, is not a matter of concern where service rates are set on an aggregated or system-wide basis. Where multiple jurisdictions are involved, the cost of specific service properties, such as distribution properties, may be identified and disaggregated, but power supply costs of power production plants and transmission lines are allocated as they usually cannot be disaggregated.

On the other hand, where specific sales are made of specific generating plant capacity and output, the specific plant costs should be determined. The FERC recognizes this principle in its use of applicable incremental capital cost rates, rather than embedded rates, for unit power sales. (The Connecticut Light and Power Company, Opinion No. 701, issued July 22, 1974, "...senior capital costs applicable to these sales should be the costs incurred by the seller during the time of construction of the specific facilities". Also, see Delmarva Power and Light Company, Opinion in Docket No. ER80-225 issued July 2, 1980).

Here, the FERC formula for AFUDC, when applied to Plant Farley, fails to measure the full cost of its construction. If that cost is used as a basis for establishing the sales price, APCO's remaining customers will be deprived of the full benefits of lower money costs actually used to construct property remaining in their service.

Therefore, the debt and preferred stock components of AFUDC on Plant Farley should be adjusted to include as nearly as possible the actual costs of those funds raised during the construction period. An appropriate, corresponding adjustment should also be made to the income tax component of a purchase price to reflect the fact that the preferred stock rate is an after-tax rate and must be expanded by the appropriate tax expansion factor.

A similar adjustment, including income tax expansion of the after-tax rate, may also be required to the cost of common equity funds used during construction. As previously stated, the return on common equity included in the AFUDC formula prescribed by the FERC is limited to that last granted by the primary rate regulator (Alabama). To the extent actual costs of common equity capital during the construction period exceeds that rate permitted in the FERC formula, an adjustment to the common equity component of AFUDC is appropriate.

Furthermore, the FERC formula for computing AFUDC provides for the compounding of the rate twice each year, in the same manner that interest on a savings account is applied to the entire balance of the account, including interest previously earned and credited.

The AFUDC reflected on the books of APCO does not fully consider these compounding effects. Clearly, it is necessary to finance the carrying costs of a construction investment not earning a current cash return just as it is necessary to finance the other costs of construction, such as labor and materials. Thus, an adjustment to fully reflect such compounding is appropriate.

ITEM 4: Loss of Tax Deferrals from Book-Tax Depreciation Life Differences and Construction Overheads

There are several factors that result in the need for further adjustments to the recorded book cost of plant when the "recorded cost" is used as a basis to establish the sales price of an asset. These adjustments are related to the differing tax treatments allowed under the income tax regulations and the regulatory treatment of the tax benefits.

Under the regulations, a utility, such as APCO, could elect to accelerate the deduction of depreciation for income tax purposes. In order to receive this treatment for depreciation, APCO was required to establish separate accounts to accumulate the tax effect of these accelerated deductions (accumulated deferred income taxes). This treatment was only required for the "method" difference or the difference between the accelerated method and the "tax straight-line" depreciation based on the Asset Depreciation Range (ADR) Median Life. The difference between this "tax straight-line" depreciation and book depreciation (excluding basis

differences) -- the "life difference" -- could be treated as an immediate reduction in income tax expense for rate regulatory purposes, without a corresponding provision for deferred income taxes.

This "life difference" was in fact treated as a reduction in income tax expense both in the FERC and APSC rate regulatory process. Ratepayers actually received approximately a $2 rate reduction for each $1 of tax reduction, because of the tax expansion factor. Under this "flow-through" process the rates set are reduced during the early portion of the assets' life on the basis that in future years, when these differences reverse (and they will reverse) the rates set will be higher by the amount of the related income taxes. However, when the plant, or a portion thereof, is sold, the reversal is immediate. Therefore, when an asset is sold at recorded book cost, the difference between book cost and its related tax basis will produce taxable income. In this situation, there are no taxes provided to offset the reversal of the taxes and, accordingly, an additional recognition of income taxes is necessary in establishing the sales price.

As an illustration, if the recorded book and tax cost are identical at the in-service date -- say $10,000 -- and straight-line depreciation is used for both regulatory and income tax reporting purposes but the tax life is 2 years and the book life is 5 years, an adjustment to "recorded book" costs is needed in the amount of $5,427, if the property is sold at the end of the second year. This amount is shown in the following example:

	Book Basis	Tax Basis	Differences
Original cost	$10,000	$10,000	$ -
Less- Accumulated depreciation			
Book [($10,000 ÷ 5 years) x 2 years]	(4,000)		
Tax [($10,000 ÷ 2 years) x 2 years]		(10,000)	6,000
	$ 6,000	$ -	$ 6,000
Flow through of tax benefits at 47.4923%			$ 2,850
Income tax expansion factor			1.90448
Prior reductions in revenue requirements			$ 5,427

Computation of gain (loss) on sale and income taxes due	Sale at Recorded Cost Only	Sale at Recorded Cost Plus Tax Adjustment	Difference
Sales price	$6,000	$11,427	$5,427
Less- Tax basis	-	-	-
Taxable gain	$6,000	$11,427	$5,427
Tax at 47.4923%	2,850	5,427	2,577
Capital recovered after tax	$3,150	$ 6,000	$2,850
Book cost	6,000	6,000	-
Short-fall in recovery of book cost	$2,850	$ -	$2,850

Without a recognition of this adjustment, the Company would not be allowed a recovery of its recorded investment in plant to the detriment of its remaining customers and investors.

A similar adjustment is needed to reflect the treatment afforded certain overhead costs capitalized as part of the plant cost. For a period of time, the Company was deducting certain overhead costs (pensions, payroll, taxes, etc.) currently for income tax purposes and capitalizing these costs for accounting and regulatory purposes. The tax benefits of this deduction were "flowed through" during the construction period and will reverse (as does the depreciation life difference) when the plant, or portion thereof, is sold. Thus, absent this adjustment, APCO will not recover its actual costs of constructing Plant Farley.

ITEM 5: Reduction in Income Taxes on Sale Because of Availability of Capital Gains Treatment

In the previous sections of this Affidavit, the tax impact of the sale has been discussed in terms of the statutory income tax rate related to "ordinary income". However, a portion of the difference between the tax basis and the ultimate sales price will be taxed at lower capital gains rates for Federal income tax purposes. To the extent that the income tax effects of timing differences have been previously treated on a "flow-through" treatment for rate-setting purposes (Item 4), the reversal of these amounts will result in a gain which will be taxed partially at ordinary income tax rates (composite Federal and state income tax rate of 47.4923%) and partially at capital gain tax rates (composite Federal and state income tax rate of 29.9898%).

To the extent income taxes have been previously provided to offset the income taxes resulting from the reversal of those normalized timing differences upon the sale, no additional provision for income taxes needs to be considered in establishing the sales price. However, to the extent previously deferred taxes exceed the resulting tax liabilities arising from the sale, (due to the lower capital gains tax rate) these taxes should be used to reduce other taxes resulting from the sale. This treatment results in the purchaser paying the income taxes arising from the sale only at those rates actually applicable to that tax gain on the sale.

It is also to be noted, however, that all income tax effects will remain uncertain for some period of time. Therefore, the mechanics for subsequent adjustments and true-up of all income tax effects should be considered as part of the sales arrangement.

IV. CONCLUSION

In conclusion, if the objective is to determine APCO's actual costs relating to Plant Farley, to the extent that those costs can be determined on an accounting basis, it would be incorrect to rely on the cost recorded for Plant Farley on APCO's books without making the adjustments that I have described. These adjustments are essential for recovery of the accounting costs that are indisputably attributable to Plant Farley.

UNITED STATES OF AMERICA

BEFORE THE

NUCLEAR REGULATORY COMMISSION

STATE OF ALABAMA)

JEFFERSON COUNTY)

RICHARD WALKER, being first duly sworn, deposes and says that he has read the Affidavit of Richard Walker and that the matters and things set forth therein are true and correct to the best of his knowledge, information and belief.

Richard Walker

Richard Walker

Subscribed and sworn to before me
this the 12th day of October, 1984.

Ellen P. Kilson

Notary Public

My Commission Expires: 5-30-87

CHRONOLOGY OF MAJOR EFFORTS TO COMPLY WITH LICENSE CONDITIONS

MAJOR ITEMS BY DATE		MONTH/YEAR		EFFORTS DURING INTERIM
		1/1977		
INITIAL LICENSE CONDITION...	6/25/77			
APCO TO AEC - UNIT POWER SALE PROPOSAL...	10/27/77			
AEC TO APCO - LETTER STATING AEC WAS REVIEWING PROPOSAL AND WOULD RESPOND	11/14/77		*	
		1/1978	*	
		1/1979	*	
		1/1980	*	
		1/1981	*	
LICENSE CONDITION REVISED BY ALAB TO OWNERSHIP SHARE..	6/30/81		**	APCO SEEKS STAY OF LICENSE PENDING APPEAL
AEC TO APCO- REQUESTING DETAILED COST DATA...	7/17/81		**	APCO TO AEC - PREMATURE TO INITIATE DISCUSSIONS IN VIEW OF STAY
NRC ISSUED AMENDMENTS TO LICENSES...	8/10/81		**	
NRC DENIES STAY..; AEC TO APCO - REQUEST DATA...	10/22,23/81		**	APCO INVESTIGATES OTHER JOINT OWNERSHIP ARRANGEMENTS
11TH CIRCUIT COURT DENIAL OF STAY...	1/20/82	1/1982		APCO COMPLIES WITH DATA REQUESTS OF AEC: • APCO TRANSMITS READILY AVAILABLE DATA TO AEC • APCO OFFERS AEC TO VISIT APCO FOR BULK DATA
APCO TO AEC-REQUEST BASIC INFO. FOR DISCUSSIONS...	5/6/82			AEC REQUESTS ADDITIONAL DATA
AEC TO APCO - AEC WILL CONTACT APCO WHEN READY FOR DISCUSSIONS	6/4/82		*	
			*	APCO DEVELOPS PROPOSAL
		1/1983	*	AEC VISITS APCO FOR BULK DATA APCO TRANSMITS DATA TO AEC
MEETING OF 5/24/83 SET FOR DISCUSSIONS...	3/ /83			
APCO JOINT OWNERSHIP PROPOSAL...	4/29/83		*	
AEC TO APCO - INITIAL RESPONSE TO PROPOSAL...	5/24/83		*	
APCO TO AEC - SUMMARY OF NEGOTIATING POSITIONS..	9/26/83		*	
AEC TO APCO - PARTIAL RESPONSE TO SUMMARY...	10/11/83		*	
AEC TO APCO - PROPOSAL TO APCO...	1/20/84	1/1984	**	APCO/AEC NEGOTIATIONS
			**	APCO PREPARES DETAILED PURCHASE AND OWNERSHIP, OPERATING & NUCLEAR FUEL PROPOSALS
APCO TO AEC - DETAILED PURCHASE PROPOSAL(EXCL. PRICE).	4/11/84		*	
MEETING ON PRICE ISSUE...; APCO TO AEC - DETAILED OPERATING AND FUEL PROPOSAL	6/84		*	

* APCO AWAITING AEC
** AEC AWAITING APCO