PRIVATIZATION OF THE U.S. ENRICHMENT CORPORATION AND ITS IMPACT ON THE DOMESTIC URANIUM INDUSTRY

HEARING

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SUBCOMMITTEE ON
OVERSIGHT AND INVESTIGATIONS

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PRIVATIZATION OF THE U.S. ENRICHMENT CORPORATION AND ITS IMPACT ON THE DOMESTIC URANIUM INDUSTRY

THURSDAY, APRIL 13, 2000

HOUSE OF REPRESENTATIVES,
COMMITTEE ON COMMERCE,
SUBCOMMITTEE ON OVERSIGHT AND INVESTIGATIONS,
Washington, DC.

The subcommittee met, pursuant to notice, at 3 p.m., in room 2123, Rayburn House Office Building, Hon. Richard Burr (vice chairman) presiding.

Members present: Representatives Barton, Burr, Bilbray, Whitfield, Bryant, Stupak, Green, and Strickland.

Also present: Representative Wilson.

Staff present: Dwight Cates, majority investigator; Amy Davidge, legislative clerk; and Edith Holleman, minority counsel.

Mr. BURR. At this time, the Chair would call to order the Subcommittee on Oversight and Investigations hearing, a review of the U.S. Enrichment Corporation's privatization and its impact on the domestic uranium industry. At this time the Chair would recognize himself for an opening statement. The Portsmouth and Paducah gaseous diffusion plants were built by the Atomic Energy Commission in the 1950's for the purposes of enriching uranium for defense needs. In the 1960's, the plants were no longer required for bomb production and their mission shifted to meet fuel demands of the nuclear power industry.

For decades, the government controlled this uranium production. However, in the early 1990's, it became increasingly clear to Congress that the government had no business controlling an enterprise which markets its services exclusively to the private sector. In response to the 1992 Energy Policy Act, in 1993 the enrichment enterprise was transferred from the Department of Energy to a newly formed government-owned corporation called the United States Enrichment Corporation. Pursuant to the USEC Privatization Act of 1996, the Clinton administration, led by the Treasury Department, determined that the complete transfer of the government's interest in USEC through an initial public offering of stock met all the statutory criteria set out by Congress. The IPO stock sale was completed in July, 1998.

The committee began its review of USEC's privatization and the impact it has had on the uranium industry 12 months ago. This committee is interested in whether the Clinton administration followed the law when it privatized USEC and whether USEC has

lived up to its ongoing agreement with the government, agreements it freely entered into before privatization.

The committee has also focused on USEC's activities as executive agent to the Russian Highly Enriched Uranium Agreement, a critical nuclear non-proliferation agreement. The administration has said as recently as today's Wall Street Journal senior administration official was quoted, it only followed the directions of Congress in privatizing USEC. I wish it were that simple. Congress most certainly did provide direction to the administration, but I question whether the administration actually followed those directions.

I have a few things I am interested in and would like to hear from our witnesses about. I have a number of concerns about the role played by executive branch agencies in USEC's privatization. The Department of Energy transferred a large amount of natural uranium to USEC a few weeks before privatization. According to the Department, these transfers really didn't amount to much but according to the uranium industry, USEC's subsequent sale of this uranium has hurt their viability.

If this is true, then the Clinton administration clearly acted outside the terms of the USEC Privatization Act of 1996 which required that the manner of privatization chosen by the administration ensures the viability of the uranium mining and conversion service industries. I would like to know what the Treasury knew about the financial health of USEC and the enrichment industry when it decided to privatize USEC through the stock sale. It appears that Treasury and its financial advisors relied primarily on information provided by USEC.

I am concerned that USEC did not make it clear to Treasury or to stock investors that the market price of uranium was trending down and USEC's production costs were trending up indicating future viability was not certain. There are many complicated and wide ranging issues to discuss today. I look forward to the testimony of all of our witnesses.

At this time, I would recognize the ranking member, Mr. Stupak, for an opening statement.

Mr. STUPAK. Thank you, Mr. Chairman. I want to thank you for holding this hearing. It is long overdue. The legislation authorizing a privatization of the U.S. Enrichment Corporation, USEC, came from this committee. But when the actual agreement was proposed and resulted in much skepticism from the press, this committee had held no oversight. Nor do I believe that the administration did an independent review it was tasked with before letting a public offering occur.

Even today, the Treasury Department, which set up this deal and is now faced with the reality of junk bond rating which in effect would allow USEC to shut down a plant, seems reluctant to do the essential review. Oversight before privatization might have avoided some of the problems we are facing today because they were publicly identified at the time. It was well known that there was an overcapacity of enrichment services and that prices were dropping to below USEC's cost of production and escalating price of the Russian product. It was known that the power prices in the United States were increasing, not dropping, and that an expectation of obtaining power costs lower than the government's sub-

sidized contract USEC probably were not realistic. Currently, power costs make up 50 percent of the production costs.

There are many, many questions about the viability of the proposed next generation technology that should have been fully debated. But at the time, of all the agencies that were required to declare that USEC display economic viability as required by Congress, only Commerce had the foresight to state, "Commerce emphasized that any in-depth analysis on its part award privatization of USEC through an IPO, initial public offering, meets the statutory criteria would require great speculation as to the future of the suspension agreements as well as the future market and political conditions."

The Nuclear Regulatory Commission which was tasked by Congress to determine if a reliable and economic domestic source of uranium rich services would be provided was told by the USEC board that an investment-grade credit rating was the only criteria it should look at. Since USEC had received that rating, the NRC washed its hands of any further responsibility. So much for independence. Oversight might have avoided the loss as sustained by the uranium industry because of what it alleges were illegal transfers of uranium by the Department of Energy to USEC and the illegal sales of the uranium in a manner that has almost destroyed the domestic industry. Oversight might well have helped avoid multimillion dollar losses suffered by the stock and bond holders because they were not fully aware of the market and technology realities. It might have avoided the privatization completely by forcing a closer look at the long-term economics of the deal. It might have avoided the overselling of and overreliance of an unproven technology that at best was still less economical than that of competing producers and at worse was a bottomless pit from which little would emerge. It might have forced USEC to have a credible backup plan if its technology choice failed, a plan that could have been implemented immediately.

If that had been done, USEC would not be here today. Nine months after pulling the plug on its failed technology with no clear path to go forward, generating the majority of their cash-flow by dumping cheap uranium on a market and selling its unused power contracts at a profit that would both junk stocks and junk bonds. If oversight had been done, the administration would not be here today also with no clear path forward. The provision of nuclear fuel to our defense and energy industry is essentially a government function. The government and this body cannot wash its hands of its responsibility. Nor can the U.S. Enrichment Corporation be allowed to run a company into the ground because of bad business and financial judgments on the theory that the government must bail it out because it plays such an important role in our nation's defense.

A recent report rating USEC's $500 million in junk bond says that they are a good buy because the government won't let the corporation fail. We should not be in a position to be held hostage by incompetent but highly paid management for their personal and their stockholders' benefit. I must say that in a real company, if a chairman and board allowed their stock to lose two-thirds of its value and their bonds to go below the investment rating and has

no serious plan for recovery, that they would very likely have been gone by now. The chairman of a serious company asking for government assistance will start by cutting their own salary much as Lee Iacocca did many years ago.

This matter, Mr. Chairman, requires more than one hearing if we are going to have any real impact. USEC is partly our creation and it is our responsibility to make sure the legislation is carried out. With that, Mr. Chairman, I yield back my time.

Mr. BURR. The gentleman's time has expired. The Chair would recognize the gentleman from Kentucky, Mr. Whitfield, for an opening statement.

Mr. WHITFIELD. Mr. Chairman, thank you very much. We appreciate Chairman Bliley agreeing to this hearing which we consider particularly important at this time. Events surrounding the two plants, the one in Paducah in my district and the one in Piketon, Ohio in Congressman Ted Strickland's district have both been the subject of extensive media coverage and numerous House and Senate hearings over the last year. Those hearings, including a previous hearing by this subcommittee, focused on revelations about worker exposure to contaminated materials without their knowledge, the results of DOE investigations about warter safety and environmental damage at the plants and in the surrounding communities, proposed budgets affecting plan operations, and the need for a newly established Federal program to compensate workers or their surviving family members for illnesses they contracted while exposed to hazardous materials and chemicals used in the enrichment process.

Although USEC is a private corporation, it is the only company in the United States which enriches uranium to fuel nuclear power plants and the only company designated as the U.S. agent in a nuclear disarmament arrangement with the Russians. Therefore, USEC's future is important both in terms of our national security interests and because nuclear power supplies 20 percent of this Nation's electricity. Congress has a responsibility to obtain the facts surrounding USEC's financial condition.

Rumors in the communities of Paducah and Portsmouth as well as on Wall Street about possible plant closures and the financial status of USEC and also concerns expressed by institutional investors and independent financial analysts make this hearing imperative. Some are saying the government should assume responsibility for the operation of the two plants. Some are forecasting such serious financial problems in the long run for USEC that it may be necessary to find a merger or acquisition partner even though the law which privatized USEC prohibits any one entity from owning more than 10 percent of the company.

Some say that USEC loses money serving as the government's executive agent of the Russian enrich uranium while others say the company makes money off this arrangement. These are just a few of the issues raised by interested parties directly impacted by USEC's ability to remain competitive. So our purpose today is to obtain some facts. We already know some of them. USEC did announce the layoff of 850 workers at Paducah and Portsmouth. Moody's and Standard & Poor's have downgraded the credit rating of USEC below investment grade so the company's corporate bonds

are now considered junk bonds. Electricity accounts for between 50 to 55 percent of USEC's production costs and the company is currently the beneficiary of power at an average cost of 2 cents per kilowatt hour.

The Paducah and Portsmouth plants are currently operating at 25 to 35 percent capacity. SWU market share end prices are falling. USEC's net income has fallen from $360 million approximately 5 years ago to a projected $35 million next year. As production decreases, costs per SWU increase. The NRC has launched its own investigation into the economic viability of USEC. Dividend payouts to stockholders have been reduced by 50 percent. It appears that the company may be using its free cash-flow to buy back outstanding shares of stock. All of this sounds quite ominous but is it? We hope to find out today from our panel of witnesses what are the real problems and are there some solutions.

Let me close by saying this hearing is not just about jobs. Regardless of what the future may hold for USEC, our government cannot let this industry fail. We must have a domestic supply of enriched uranium to meet our energy needs, and we must continue to demilitarize the Russian nuclear arsenal. And, of course, we are particularly interested in this hearing to determine the impact of privatization and the Russian agreement on the uranium mining and conversion service industries. Mr. Chairman, I look forward to the testimony of the witnesses.

Mr. BURR. The gentleman's time has expired. The Chair would ask unanimous consent that all members of the subcommittee be allowed to enter opening statements at any time in their entirety. At this time, hearing no objection, so ordered. At this time, the Chair would recognize the gentleman from Ohio, Mr. Strickland, for the purposes of an opening statement.

Mr. STRICKLAND. Thank you, Mr. Chairman. I look forward to this hearing. I hope it will spark a thorough and revealing debate about the Federal Government's role in the uranium enrichment industry. Thorough because I do not think that all of the stakeholders in this debate are present today. Revealing because I think we must ask some tough questions today in order to better understand the current financial condition of the United States Enrichment Corporation, how we got here, and how we move forward to ensure a reliable and economic domestic uranium mining conversion and enrichment industry.

I opposed the privatization of USEC. I was gravely concerned that designating a private USEC as the executive agent for the Russian HEU Agreement was a recipe for disaster. It made no sense to me to require an inherent governmental function to rest in the hands of a corporation responsible to its shareholders and its bottom line. I raised concerns that USEC as the executive agent of the HEU Agreement could lead the corporation to undertake actions which conflict with the statutory criteria established by Congress and threaten the viability of the uranium enrichment industry.

As the representative of the uranium enrichment facility in Piketon, Ohio, I have obviously followed USEC's course with tremendous interest, and it seems to me the corporation's priorities are wrong. In less than 2 years after privatization, USEC has al-

ready publicly debated walking away from the Russian deal. In less than 2 years, they have visited Capitol Hill offices asking for a $200 million bailout and as this industry declines, management profits.

According to the Associated Press, USEC's CEO and president receives a total compensation package of $2.48 million and has negotiated a $3.6 million golden parachute should he resign or be replaced. That same individual's salary under the public corporation was approximately $350. With these facts as a backdrop, I am proud to admit that a major concern of mine throughout the privatization process has been the effect it has had on the workers and the communities of southern Ohio.

This privatization process intertwines national security, energy security, and Wall Street issues in a complicated manner but given what we know about the personal enrichment of certain individuals, we must not forget the families in Piketon, Ohio, and Paducah, Kentucky, who fear a plant closure and brace themselves for the impact such a closure would have on the local economies. Southern Ohio and western Kentucky do not weather this transition alone. Other local communities such as Metropolis, Illinois, also feel the negative effects of privatization.

We must remember that USEC provides 75 percent of the nuclear fuel for nearly 20 percent of our nation's electricity producers. We have 103 operating nuclear power plants in this country located in 31 different States. It seems very clear to me that our Nation's energy supply depends a great deal on USEC's viability. I understand that foreign competitors offer enrichment services and conversion services, but do we want to depend on other nations for our nuclear fuel supply just like we depend on OPEC for our oil supply. I think the answer is no. I think that many of my colleagues here today will agree that the Federal Government has an obligation to safeguard this industry but not necessarily this corporation and that is why I think we should seriously look at the government once again assuming ownership of this industry.

Mr. Chairman, what we know now about privatization is that it was a classic case of massive insider enrichment. A handful of insiders got rich at the expense of national security, domestic energy security, the well-being of workers, local economies, and taxpayers.

How did it happen? It happened because every time a legitimate concern was raised, it was minimized and ignored. If personal gain overshadowed national security issues, then it is time we understand what went wrong. Mr. Whitfield and I will see over 800 workers at our facilities lose their jobs this summer and that will bring the total number of separations at the plants to nearly 1,500 workers, approximately one-third of the workforce.

If the IPO method of privatization was chosen in large part because it meant significantly fewer layoffs as I was told, then I ask who did the math. Some of our witnesses here today first blew the whistle on privatization pitfalls we are now experiencing. Still other highly regarded individuals like Dr. Thomas Nef, the father of the Russian HEU Agreement, and Senator Domenici sent shots across the bow that this privatization was potentially lethal to our national security. Too many people predicted USEC's current situation, and I hope today is not the last hearing on this issue. I also

hope it is not too late for government to step in and to do the right thing. Mr. Chairman, I have a letter from Senator Mike DeWine. He has asked if we could enter this into the record.

Mr. BURR. Without objection, so ordered.

Mr. STRICKLAND. Thank you, sir.

Mr. BURR. The gentleman's time has expired. Does the gentlemen from California have an opening statement?

Mr. BILBRAY. I have no opening statement.

Mr. BURR. Does the gentleman from Tennessee have an opening statement?

Mr. BRYANT. Thank you, Mr. Chairman. I too add my appreciation for your conducting this hearing. I appreciate the panel that we have assembled today. We will be, in my case, going in and out today because of conflicting other matters in our schedule; and I apologize in advance for that. Out of a great deal of respect for our Chairman and courtesy to the panels, I am going to take advantage of your generous offer to submit my full statement into the record and would yield back my time.

[The prepared statement of Hon. Ed Bryant follows:]

PREPARED STATEMENT OF HON. ED BRYANT, A REPRESENTATIVE IN CONGRESS FROM THE STATE OF TENNESSEE

Thank you Mr. Chairman, Mr. Chairman, I appreciate your holding this timely hearing today, and I want to welcome all of our distinguished witnesses. Because of the importance of this issue, I am very anxious to hear from the panels you've assembled today.

Mr. Chairman, the federal government has never been accused of being the most efficient operation the world has ever seen. From the military's thousand dollar toilet seats to the billions and billions of dollars lost every year in Medicare waste and fraud, the government's reputation as inefficient has been well earned.

Today, however, this subcommittee finds itself in the strange position of investigating the inefficiencies of a private company. As the *Wall Street Journal* points out in today's addition, the financially troubled United States Enrichment Corporation "may be about to close one of the nation's two remaining uranium-enrichment plants . . ." It also reports that USEC announced in February that it will reduce its workforce by 850 people and cut its annual dividend in half all in an effort to reduce costs.

Having been in the private sector before coming to Congress, I am very much aware of the fact that becoming more competitive may mean the need for periodic reductions in a company's workforce. However, a 20% reduction is a large enough cut to indicate that USEC is either burdened with a bloated workforce or that it is in very serious financial trouble. In either case, because of the national security implications of what USEC produces, the February announcement is extremely troubling.

If USEC can function more efficiently with 850 fewer employees, why, when the Treasury Department was developing the USEC privatization plan, did it apparently set this company up for failure by mandating that it maintain so many employees. On the other hand, if USEC is simply trying to jettison everything but the life boats in an attempt to remain solvent, then we need to ask what has happened in the last two years to cause this crisis? Are we looking at gross mismanagement, incompetence, or simply the harsh reality of market forces?

With a 70% drop in the price of its stock since USEC's initial public offering, I think the solvency of this company is in question. While the U.S. has not produced uranium since the 60s, uranium production is still vital to the national security of this country, and I think this subcommittee should spend its time today trying to learn as much as possible about USEC's current position so as to avoid some of the worst case scenarios.

Again, I thank the chairman for holding this hearing, I look forward to questioning the members of the assembled panels and I yield back the balance of my time.

Mr. BURR. I appreciate that from the gentleman. Does the gentleman from Texas, Mr. Green, have an opening statement?

Mr. GREEN. Mr. Chairman, I have an opening statement but I will submit it for the record.

[The prepared statement of Hon. Gene Green follows:]

PREPARED STATEMENT OF HON. GENE GREEN, A REPRESENTATIVE IN CONGRESS FROM THE STATE OF TEXAS

Thank you, Mr. Chairman for scheduling today's hearing. I look forward to the opportunity to have the testimony of the witnesses on the record on the issues that we will raise here today.

Almost two years ago, the Treasury Department, based on the recommendation of the United States Enrichment Corporation board and the agreement of several other federal agencies, approved the sale of the USEC through an initial public offering of stock (IPO). This IPO, combined with additional expenses, brought the Treasury over $1.8 billion in revenue. The future seemed bright.

Now, however, the picture is muddled. Despite the seemingly rosy forecast that existed at the time, current conditions, according to USEC, are dire. The stock price has fallen from over $14 at the IPO to just under $5 as of last week. USEC's credit rating has been downgraded by Standard and Poor's to junk-bond status. The company has announced plans to terminate 850 employees in June of this year, on top of the 500 it has already let go since privatization. Additionally, USEC is said to be considering closing one of the two gaseous diffusion plants (GDPs) prior to 2005, which may or may not be a violation of the privatization agreement.

Further, the damage is not limited solely to USEC. When privatized, the Department of Energy (DOE) transferred stockpiles of unenriched uranium to the corporation. In an attempt to generate cash flow, USEC has since sold those stockpiles on the open market, threatening the viability of the domestic uranium mining industry.

Finally, the troubles with USEC have threatened our national security. When USEC was privatized, they willingly assumed the role as the executive agent for the HEU Agreement, under which we purchase uranium from dismantled Russian nuclear warheads and reprocess it for use in the commercial market. This agreement not only allowed USEC to control the flow of uranium out of Russia, one of the only other world producers, but ensured that Russian weapons-grade uranium did not make its way into the hands of undesirable nations or organizations.

Last November, USEC threatened to pull out of this agreement unless the U.S. government paid it $200 million dollars over the next two years. After DOE examined and raised questions about that request, the corporation backed down and agreed to continue with the agreement. The threat, however, combined with the financial straits faced by USEC, raise alarm and concern about the future of the HEU Agreement.

Today, Mr. Chairman, I hope that we can start down the road to discovering where we went wrong with the United States Enrichment Corporation. Did we choose the wrong time for privatization? Could anyone have foreseen some of these events, such as a drop in the price of enriched uranium on the world markets? Is government intervention or a bailout of the corporation necessary? Maybe we should buy back the corporation if it benefits taxpayers. Who, if anyone, is to blame for the mess that we have before us today? I hope that we will find the answers to these and other questions, if not today, then in the near future.

Again, I would like to thank the witnesses for appearing today and I look forward to their testimony.

Mr. BURR. The Chair also appreciates Mr. Green's request. The Chair would ask unanimous consent that Mrs. Wilson be allowed to provide an opening statement even though she is not a member of the subcommittee but is a member of the full committee. Without objection, the Chair would recognize Mrs. Wilson for an opening statement.

Mrs. WILSON. Thank you, Mr. Chairman. I appreciate your forbearance in allowing me to participate in this hearing today. I think this hearing is not only about the management of the U.S. Enrichment Corporation but it is also about what can be done to save the front end of the domestic nuclear fuel cycle.

My State of New Mexico has been the leading producer of uranium since the 1950's. Today we are no longer producing uranium to fuel almost one quarter of our electric needs in the nuclear power industry. This is unacceptable energy policy. The domestic uranium industry has been forced to compete with Russian and U.S. uranium stockpiles available for commercial use since the end of the cold war.

Our Nation's non-proliferation policy calls for the Russian stocks to be absorbed by the commercial market in competition with our domestic producers. In 1996, these producers thought they had worked with Congress to meter in the government uranium in a way that would keep the price of uranium reasonable and, to the extent possible, maximize the value of the government reserves. However, Congress and the producers were surprised to learn shortly before USEC's privatization that the government corporation had amassed huge amounts of natural uranium and planned to sell this material with its enriched product at a very aggressive pace.

These sales of national uranium have resulted in a drop of uranium prices from over $15 in 1996 to almost $9 today. This policy is driving our producers to the brink of extinction. This has all occurred even though Congress has twice directed DOE to only sell its surplus uranium if it would not have an adverse impact on domestic producers. Mr. Chairman, I look forward to working with you and others on this committee to fix this problem. It is extremely important to me and to our Nation, and I thank you for allowing me to participate in this important hearing. I yield the balance of my time.

Mr. BURR. The gentlelady's time has expired. For what purpose does the gentleman from California——

Mr. BILBRAY. To address the committee, Mr. Chairman. An opening statement I wasn't going to make. I just want to point out to all my colleagues here as we get our testimony about this issue, it is such a habit for those of us on this side of the counter to be pointing fingers and saying what is or isn't being done or should have been done. I just want to point out that this Congress, both Republicans and Democrats in the past have not supported the export of technologies that might have helped to mitigate this problem.

Let me give you an example. Americans—American manufacturers have the capability of producing gas reactors, nuclear reactors that would convert weapons-grade uranium into power generation in the past Soviet Union in Russia. The capability of actually encouraging the past Soviet republics to use their weapons-grade material for their domestic energy generation is something that we basically walked away from and we did that starting in 1985—I mean 1995 and we sort of—the fact is it wasn't popular to talk about nuclear technology either if you are Republican or Democrat.

And I only want to raise this because we have commodities out there in the world market. And when we do not encourage our new friends to utilize those commodities for their own domestic use, they obviously are going to put that into the world market; and it is going to have impacts on the available price of certain commodities. And I just brought that up, but there is an example where

those of us in Congress could have done more and helped mitigate this to some degree. There would have been less Soviet material out there to flood the market if I can use that term because the ex-Soviet would have been using that to generate their own clean, non-greenhouse gas creating power and also not sending this material into our market. I yield back, Mr. Chairman.

Mr. BURR. The gentleman's time is expired. The gentleman raises a very valid point.

[Additional statement submitted for the record follows:]

PREPARED STATEMENT OF HON. TOM BLILEY, CHAIRMAN, COMMITTEE ON COMMERCE

Today we will review the privatization of the United States Enrichment Corporation and the impact privatization has had on the domestic uranium industry. USEC serves an important role in our domestic energy needs—it is the only domestic source of enriched uranium. USEC provides 70% of the enriched uranium used in our nuclear power reactors. A healthy USEC, and a healthy domestic uranium industry reduces our reliance on foreign countries for our energy needs. USEC also acts as the government's Executive Agent to the Russian HEU Agreement. As Executive Agent to this critical non-proliferation agreement, USEC purchases uranium from dismantled warheads that were once aimed at our country and resells this uranium as nuclear fuel for a profit.

I supported legislation that called on the Clinton Administration to bring the efficiencies of the private sector to the government-owned uranium enrichment enterprise. In passing the USEC Privatization Act of 1996, Congress supported the concept of privatization but only if certain conditions were first met, namely that privatization would not adversely affect the uranium industry or national security. We charged the Administration with making those determinations and relied on its findings. The Treasury Department completed USEC privatization in July of 1998, and everyone seemed happy with the big return we got from the sale of USEC stock.

Today, less than two years after privatization, USEC is in bad financial shape, the outlook for the uranium industry is very bad, and the Russian HEU Agreement is in jeopardy. We will never know if these troubling developments could have been avoided had the Administration chosen to privatize USEC in an alternative manner. But I do know that the path forward chosen by the Administration has had serious adverse consequences for the uranium industry and our national security.

Considering the quick decline in USEC's financial condition so soon after privatization, it is entirely appropriate for Congress to assess what information USEC provided Treasury before privatization, and what decisions the Clinton Administration made in its efforts to privatize USEC. We must evaluate whether certain facts and concerns were swept aside in the Administration's rush to sell USEC stock. For instance, before privatization USEC promised to replace its aging and inefficient enrichment plants with a low-cost alternative. But today, USEC's long term viability is in question because its plans for a new enrichment plant fell through, and it has not come up with an alternative.

Additionally, we must evaluate the impact USEC has had on the uranium mining and conversion service industries since privatization. We will hear testimony today that USEC has engaged in aggressive marketing tactics that have undercut the viability of these industries. Additionally, because the Clinton Administration has failed to adequately oversee USEC's activities as Executive Agent to the Russia deal, Congress must also step in to review the status of this critical non-proliferation agreement.

In the end, USEC's problems must be solved by USEC. If the company is unable to survive, there is little Congress can do to make it survive. However, a viable domestic uranium industry is essential for the country's long term energy needs. The nuclear energy community, particularly nuclear power companies, better start thinking hard about whether USEC will survive. What would happen if the only domestic source of enriched uranium no longer existed? Similarly, the government must decide what our future uranium needs are, and develop a plan which ensures those needs are met. Unfortunately, the Clinton/Gore Administration has not thought much about these issues, and is has no plan.

I expect today's testimony to help the Committee understand whether the Clinton Administration privatized this company in a manner that set USEC up for failure. I also expect this hearing will help me understand whether USEC is committed to long term survival, and whether the uranium industry can survive. After this hearing, I will continue to monitor USEC's financial outlook, but I will focus on the na-

tional security issues related to USEC privatization. I plan to schedule another hearing later this year regarding national security issues. I will be working closely with Representative Whitfield on these very important issues today, and in the future. Thank you, and I yield back.

Mr. BURR. At this time, the Chair would call up Mr. Timbers who is our witness on the first panel. Mr. Timbers, you are aware that this subcommittee is an investigative subcommittee and as such it has had the practice of taking in testimony under oath. Do you have any objection to taking testimony under oath?

Mr. TIMBERS. No.

Mr. BURR. The Chair then advises you that under the rules of the House and the rules of the committee, you are entitled to be advised by counsel. Do you desire to be advised by counsel?

Mr. TIMBERS. No.

Mr. BURR. I would ask you to rise with me and take the oath.

[Witness sworn.]

Mr. BURR. The Chair would recognize Mr. Timbers for 5 minutes for purposes of his opening statement.

TESTIMONY OF WILLIAM H. TIMBERS, PRESIDENT AND CEO, USEC, INC.

Mr. TIMBERS. Mr. Chairman, members of the committee, my name is William Timbers; and I am the president and chief executive officer of USEC, Inc., and its subsidiary, the United States Enrichment Corporation. Thank you for the opportunity to participate in this hearing concerning USEC which was privatized by the government nearly 2 years ago.

Privatization of the government's uranium enrichment operation was a congressional objective for some 30 years and 14 consecutive congresses. A bipartisan member—group of members on this committee and in the Senate led these efforts. It also took the efforts of the Nixon, Ford, carter, Reagan, Bush, and Clinton administrations to complete the job. As a demonstration of continuing bipartisanship and bicameral cooperation, this was truly a landmark accomplishment. The 1992 Energy Policy Act recognized that the government's uranium enrichment enterprise was failing and that life as a business in the private sector was the best hope for preserving this important domestic energy resource.

The act created the United States Enrichment Corporation, a government corporation and gave them a number of responsibilities. The act transferred all the uranium enrichment activities from the Department of Energy to the new government corporation. The act directed the new corporation to restructure the enrichment enterprise, run it like a business, make a profit, commercially implement the Russian HEU Agreement and prepare the restructured business for sale to the private sector.

The 1996 USEC Privatization Act provided the additional preparations needed for the privatization of the corporation. As directed by Congress, the USEC Federal board of directors and the Secretary of Treasury consummated the sale of USEC in July 1998 in a public offering of securities to investors. This sale became the largest privatization of Federal assets since CONRAIL yielding a total of over $3 billion to taxpayers.

On a number of occasions, I have appeared before congressional committees to report on the government's corporation's progress and prospects. Today I am here to represent USEC, Inc., a private enterprise now entirely owned by approximately 40,000 investors. As an investor-owned company, we have a fiduciary responsibility to our owners with an obligation to create shareholder value. We also continue to fulfill our national security obligation to Federal Government serving as its executive agent to implement the megatons to megawatts program on a commercial basis. And we continue as well our commitments to ensure a long-term domestic enrichment capability and to protect the health and safety of our workers.

During the 22 months since privatization, market conditions have changed dramatically. There has been a 15 percent drop in global market prices for enrichment, an 18 percent drop in global demand for enrichment, a 12 percent drop in uranium prices, and an 18 percent drop in global demand for uranium. At the same time, our costs have increased dramatically. Our summer power prices have tripled at Paducah and electricity is 55 percent of our production costs. Our cost of purchasing the Russian material has increased. Our purchase costs are now higher than our selling price. And our obligations have forced us to substantially reduce production levels resulting in higher unit costs. These and other conditions have produced a triple whammy of fewer sales, reduced revenues, and greatly increased costs.

Now, any business faced with this situation must take prompt action to change that equation. That is what we are doing, taking action; but we have had to act under a unique constraint. Let me quote to you directly from our SEC form 10-Q disclosure document dated December 31, 1999. "USEC has been constrained in responding to these market conditions by its privatization agreement with the U.S. Treasury Department. This agreement restricts the actions that USEC could take to reduce operating costs."

I am sure you can appreciate that no other business has had to contend with such changed market conditions limited by such constraints. Coming to grips with these changed market conditions means making tough decisions. These decisions and their implementation are in all of our interests. They will help us to ensure that USEC, Inc., remains a dependable, domestic supplier of enriched uranium services and retains this global leadership in a fiercely competitive business.

The workforce reduction constraints in the Treasury agreement expire this coming July. We have already announced a reduction of up to 850 employees at the Paducah and Portsmouth enrichment plants. We regret the necessity of having to lay off employees, but we must take this action to reduce costs and to make us more competitive. The fact that we are taking a hard look at all of our costs—the fact that we are taking a hard look at all of our costs to seek reductions, everything is on the table for consideration. The combined results of these factors have been a deterioration of our market, our profitability and our share price. Share price is a barometer. In USEC's case, the barometer has fallen 67 percent since the initial public offering 2 years ago. This indicates recognition by

investors of changed market conditions and the other factors I have previously mentioned.

As we stated in a public announcement last February, we expect much lower earnings for fiscal year 2001. We have also cut our dividend to investors and both Standard & Poor's and Moody's have dropped our credit rating to below investment grade. To be sure the dot com phenomenon has made the stock markets chaotic. During the past year, more than 50 percent of companies in America listed in the S&P 500 index have had their stock price decline and many well-known, respected companies have ratings below investment grade. Neither of these facts is any comfort to us or to our shareholders. The initiatives we are taking are aimed at improving both situations.

Another contributing reason for the decline in our share price is investor concern about the continuing legacy contamination issues being revealed about the Paducah and Portsmouth DOE reservations. While USEC liability in these matters was limited by the Privatization Act, some confusion exists because of the press reports. They do not clearly point out that these contamination issues arise from operational practices before USEC, Inc. was created, and they remain the responsibility of the U.S. Government.

From the day we began operations in 1993, USEC has set a high standard of commitment to safety. As directed by the Energy Policy Act, we earned certification of the plants by the U.S. Nuclear Regulatory Commission; and we are under their regulatory purview. Last September, we participated in this committee's hearings on legacy contamination issues at Paducah and Portsmouth. We clearly stated that for the benefit of our workers and host communities, we take the issues of worker protection and legacy contamination issues very seriously. We are cooperating fully with DOE as they address these historical issues. We have also taken initiatives to reinsure that current work in our plant areas is conducted safely and that we provide a strong safe working environment for our employees.

As you will recall, an NRC spokesperson also testified before your committee that day stating that NRC had determined that USEC operations were being conducted safely and our safety programs were in full compliance with their regulations. I would like to now turn to the matter of preprivatization government transfers of uranium to USEC.

Mr. BURR. Mr. Timbers, I really need to ask you to come to a conclusion. And I think all the members have had an opportunity to read your full testimony. And it certainly will be entered into the record in its entirety, but we do need to allow members on this day to try to make available your time for questions. So I would ask you to summarize if you could.

Mr. TIMBERS. Okay. I think I would like to make two final points to this. First on the Russian HEU Agreement that this has been a deal that has been successful and working for the benefit of this Nation. We are now in the sixth year of the commercial implementation of this program and that the equivalent of over 3,254 nuclear warheads have been converted to power plant fuel purchased by Russia—purchased by USEC from Russia. We have paid the Russians over $1.3 billion. Over half of that has come from a pri-

vate company partly supported by the shareholders. And we are actually ahead of the 1993 schedule.

In addition, I think it is also clear to point out that this company continues to provide a secure and dependable source of uranium enrichment. We do remain the world leader in sales of uranium enrichment services. We have a strong business fundamentals that include over $6 billion in backlog and a robust cash-flow from sales. We are a well-run, service-oriented business focused on safety, customer service, identifying and seizing opportunities, solving problems and producing results. While we are a work in progress, we have been making progress. To fulfill the promise of a privatized USEC, all concerns have to realize that the cold war is over and the war we are now fighting is global competition. Thank you, Mr. Chairman. I will submit the rest of the testimony for the record.

[The prepared statement of William H. Timbers follows:]

PREPARED STATEMENT OF WILLIAM H. TIMBERS, PRESIDENT AND CEO, USEC INC.

Mr. Chairman and Members of the Committee. My name is William H. Timbers, and I am President and Chief Executive Officer of USEC Inc. and its subsidiary, the United States Enrichment Corporation.

Thank you for the opportunity to participate in this hearing concerning USEC, which was privatized by the government nearly two years ago.

The privatization of the government's uranium enrichment operations was a Congressional objective for some thirty years and fourteen consecutive Congresses. A bipartisan group of Members on this Committee and in the Senate led these efforts. It also took the efforts of the Nixon, Ford, Carter, Reagan, Bush and Clinton Administrations to complete the job. As a demonstration of continuing bipartisan and bicameral cooperation, this was a truly a landmark accomplishment.

The 1992 Energy Policy Act recognized that the government's uranium enrichment enterprise was failing and that life as a business in the private sector was the best hope for preserving this important domestic energy resource. The Act created the United States Enrichment Corporation, a government corporation, and gave it a number of responsibilities. The Act transferred all uranium enrichment activities from the Department of Energy to the new government corporation.

The Act directed the new corporation to restructure the enrichment enterprise, run it like a business, make a profit, commercially implement the Russian HEU agreement and prepare the restructured business for sale to the private sector.

The 1996 USEC Privatization Act provided the additional preparations needed for the privatization of the corporation. As directed by the Congress, the USEC Federal Board of Directors and the Secretary of the Treasury consummated the sale of USEC in July 1998 by a public offering of securities to investors. This sale became the largest privatization of a federal asset since Conrail, yielding a total of over $3 billion to taxpayers.

On a number of occasions, I have appeared before Congressional committees to report on the government corporation's progress and prospects. Today, I am here to represent USEC Inc. as a private enterprise, now entirely owned by approximately 40,000 investors.

As an investor-owned company, we have a fiduciary responsibility to our owners with an obligation to create shareholder value. We also continue to fulfill our national security obligation to the federal government, serving as its Executive Agent to implement the Megatons to Megawatts program on a commercial basis. And we continue, as well, our commitments to ensure a long-term domestic enrichment capability and to protect the health and safety of our workers.

USEC BUSINESS CHALLENGES

During the 22 months since privatization, market conditions have changed drastically. There have been:

- A 15 percent drop in global market prices for enrichment
- An 18 percent drop in global demand for enrichment
- A 12 percent drop in uranium prices
- An 18 percent drop in global demand for uranium

At the same time our costs have increased dramatically:

- Our summer power prices have tripled at Paducah—and electricity is 55 percent of our production cost,
- Our cost of purchasing the Russian material has increased—our purchase costs are now higher than our selling price, and
- Our obligations have forced us to substantially reduce production levels, resulting in higher unit costs.

These and other conditions have produced a triple-whammy of fewer sales, reduced revenues and greatly increased costs. Any business faced with this situation must take prompt action to change that equation. That's what we are doing—taking action. But we have had to act under a unique constraint.

Let me quote to you directly from our SEC form 10Q disclosure document dated December 31, 1999. "USEC has been constrained in responding to these market conditions by its privatization agreement with the U.S. Treasury Department. This agreement restricts the actions that USEC could take to reduce operating costs." I am sure you can appreciate that no other business has had to contend with such changed market conditions while limited by such constraints.

Coming to grips with these changed market conditions means making tough decisions. These decisions and their implementation are in all of our interests. They will help to ensure that USEC Inc. remains a dependable domestic supplier of enriched uranium services and retains its global leadership in a fiercely competitive business.

The workforce reduction constraints in the Treasury agreement expire this coming July. We have already announced a reduction of up to 850 employees at the Paducah and Portsmouth enrichment plants. We regret the necessity of having to lay off employees. But we must take this action to reduce costs to make us more competitive. The fact is that we are taking a hard look at all of our costs to seek reductions. Everything is on the table for consideration.

The combined results of these factors have been a deterioration of our market, our profitability and our share price. Share price is a barometer. In USEC's case, the barometer has fallen 67 percent since the initial public offering two years ago. This indicates recognition by investors of changed market conditions and the other factors I previously mentioned.

As we stated in our public announcement last February, we expect much lower earnings for fiscal year 2001. We have also cut our dividend to investors, and both Standard and Poor and Moody's have dropped our credit rating to below investment grade. To be sure, the dot com phenomenon has made the stock markets chaotic. During the past year, more than 50 percent of the companies in America listed in the S&P 500 index had stock price declines, and many well-known and respected companies have ratings below investment grade. Neither of these facts is of any comfort to us or to our shareholders. The initiatives we are taking are aimed at improving both situations.

Another contributing reason for the decline in our share price is investor concern about the continuing legacy contamination issues being revealed about the Paducah and Portsmouth DOE reservations. While USEC liability in these matters was limited by the Privatization Act, some confusion exists because press reports do not clearly point out that these contamination issues arise from operational practices years before USEC Inc. was created and they remain the responsibility of the U. S. Government.

OUR COMMITMENT TO SAFETY

From the day we began operations in 1993, USEC has set a high standard of commitment to safety. As directed by the Energy Policy Act, we earned certification of the plants by the U.S. Nuclear Regulatory Commission, and we are under their regulatory purview. Last September, we participated in this Committee's hearings on legacy contamination issues at Paducah and Portsmouth. We clearly stated that, for the benefit of our workers and host communities, we take these issues of worker protection and legacy contamination very seriously.

We are cooperating fully with DOE as they address these historical issues. We have also taken initiatives to re-ensure that current work in our plant areas is conducted safely and that we provide a safe working environment for our employees. As you will recall, an NRC spokesperson also testified before your Committee that day, stating that NRC had determined that USEC operations were being conducted safely and that our safety program was in full compliance with their regulations.

USEC URANIUM INVENTORIES

I would like to now turn to the matter of the pre-privatization government transfers of uranium to USEC and our sale of this material. Let me summarize the situation. Uranium was transferred to USEC by the government as directed by the En-

ergy Policy Act of 1992 and the USEC Privatization Act of 1996, and information on the transfers was publicly reported.

I have made commitments to the U.S. government that USEC would limit its sales of its uranium, and I also gave assurances that our sales would be made in a market-sensitive manner. We have lived up to those commitments. I would also point out that we have a fiduciary duty to our shareholders to maximize the value of our uranium assets. Clearly, we do not want to sell our uranium in a market-disruptive manner that might lower the value of our uranium assets.

MEGATONS TO MEGAWATTS PROGRESS

We are also meeting our obligation as Executive Agent of the government by implementing the Megatons to Megawatts national security program. We are now in the sixth year of commercial implementation of the program. The equivalent of over 3,254 nuclear warheads has been converted to power plant fuel purchased by USEC from Russia. We have paid Russia over $1.3 billion thus far, and over half of that was paid by the privately owned USEC—not the taxpayer. And, we are actually ahead of the 1993 U.S./Russian schedule for purchases and deliveries. The scoreboard clearly shows that we have been successful in meeting our commitments to implement this national security program.

THE GOAL OF WORKER TRANSITION

Before concluding my remarks, I would like to return to the very important matter of workforce reductions this coming July. While these reductions will result in considerable savings, they will also result in a substantial impact on those affected employees, their families and their communities.

We have proposed that all concerned constituencies, including USEC, Congress, the Administration, DOE, the unions and the communities, work together to mitigate these impacts. Worker transition to cleanup programs is the most logical and feasible way to address this matter. We are prepared to cooperate with all constituencies to pursue a seamless worker transition. But to achieve this goal, we must put aside differences and begin working together.

I would like to conclude by expressing my appreciation to the Committee for your consideration. My five years of public service as USEC's Transition Manager, President and CEO of the government corporation have afforded me an opportunity to work with a wonderful group of employees and with many dedicated public servants in the Congress and the Administration.

As President and CEO of the private-sector USEC, I am determined that we will meet our commitments to our owners for creation of shareholder value and will fulfill our obligations and commitments to the government. I firmly believe that we can and will achieve continued profitability for our shareholders. We will continue to succeed in implementing the Megatons to Megawatts program. And we will continue to provide a secure and dependable domestic source of uranium enrichment.

We remain the world leader in sales of uranium enrichment services. We have strong business fundamentals that include over $6 billion in backlog and a robust cash flow from sales. We are a well run, service-oriented business focused on safety, customer service, identifying and seizing opportunities, solving problems and producing results.

While we are a work-in-progress, we have been making progress. To fulfill the promise of a privatized USEC, all concerned have to realize that the Cold War is over and the war we are now fighting is global competition.Thank you for your consideration. I welcome your questions.

Mr. BURR. Thank you, Mr. Timbers, for accommodating the committee, and I will assure you that we all take it with great interest, your entire testimony.

The Chair at this time would ask unanimous consent that this set of documents previously agreed to by the majority and the minority be entered into the record with the understanding that staff will work with all interested parties after this hearing to make whatever redactions that are deemed appropriate part of the documents insertion into the formal public record.

Without objection and hearing none, so ordered.

[The information referred to follows:]

USEC FINANCIAL SITUATION AND PROSPECTS
AS OF MARCH 2000

1. Introduction

The United States (U.S.) government privatized its uranium enrichment enterprise, the United States Enrichment Corporation (USEC), through an initial public offering (IPO) on July 28, 1998. The corporation was privatized as USEC Inc., through the sale of 100 million shares at $14.25 per share. The privatization committed the corporation to $500 million in debt in order to increase the final return to the government to $1.925 billion. In the 18 months since it was privatized USEC's share value has declined steadily, and is currently (March 27, 2000) valued at about $4.75 per share, 33% of its IPO price.

During the past 18 months, USEC has claimed that it was financially encumbered with: (a) a larger than necessary labor force, (b) a gaseous diffusion plant (GDP) that it did not need (Portsmouth) (c) the enrichment component (SWU) of low enriched uranium (LEU) derived from Russian highly enriched uranium (HEU) that was priced above market price and its own cost of production, and (d) an atomic vapor laser isotope separation (AVLIS) enrichment research and development (R&D) program that it could not afford to support. While the corporation's management was generally aware of the foregoing issues at the time of the IPO, the financial and political communities do not seem to have been as aware of some of them as they should have been.

Acknowledging its financial problems, USEC announced on February 3, 2000, that it would reduce its production workforce by 20% this summer, halve the company's annual dividend, and begin a new and aggressive program to repurchase an additional 20 million shares of its common stock. USEC also stated that it expects its fiscal year (FY) 2001 net income will only be about one-third of its FY 2000 net income. Not surprisingly, the union representing workers at the two GDPs, a number of USEC's customers, and several members of Congress have expressed concern about the company's viability and the potential impact of its financial difficulties. In accord with the USEC Privatization Act of 1996, the Nuclear Regulatory Commission (NRC) is now undertaking a review of USEC's financial viability following the downgrading of the company's credit rating below investment grade.

This report examines USEC's current financial situation and its future prospects. However, prior to reviewing the company's financial status, the encumbering issues referred to above are reviewed in order to provide background for the subsequent discussion.

2. Background

When it was privatized in July 1998, USEC had a workforce of approximately 5,000 people, mostly contractor employees. By November 1998, a voluntary program reduced

the workforce at the two GDPs by 259 people. A follow-on voluntary reduction campaign reduced labor by another 250 people by mid-1999. USEC took over direct operations of the GDPs from its contractors in May 1999. The termination of the AVLIS R&D program resulted in a workforce reduction at Lawrence Livermore National Laboratory (LLNL) of about 500 people during the summer of 1999. At the end of June 1999, USEC had 3,960 employees, including 3,790 at the plants (2,100 at the Portsmouth GDP and 1,690 at the Paducah GDP) and 170 at the company's headquarters in Bethesda, Maryland. On the same day that it released its second quarterly report for FY 2000 it also announced that it planned to reduce its production workforce by a further 850 people beginning in July 2000. The reduction, which will be primarily voluntary and about the same number of people at each plant, will leave USEC with a total workforce of about 3,110 people. It was stated that headquarters costs would also be reduced, presumably by some staff reductions.

As a condition of privatization, USEC committed to continuing operation of both of the gaseous diffusion plants until January 1, 2005, subject to certain criteria. The criteria pertained to unforeseeable catastrophic events, the corporation's financial health, and specific market conditions. During 1999, particularly in the second half of the year, there were concerns that USEC was planning to shutdown one of its GDPs, possibly the Portsmouth GDP, as soon as it could possibly do so. It is understood that though USEC had discussions with the NRC over the past several years, in mid-August 1999 it indicated that it planned to request certification amendments during the March-May 2000 time period. It, reportedly, planned to amend its Paducah GDP certification in order to increase the enrichment product assay limit from 2.75 weight percent (w/o) U^{235} to 5.5 w/o, by the end of 2001. In September 1999 it was reported that USEC expected to obtain NRC approvals for the upgrades by the end of September 2000. While it is understood that USEC applied for the certification amendment at the beginning of March 2000, it could be well into next year before NRC completes the certification process.

On November 14, 1996, while still a government-owned corporation, USEC, as the U.S. Executive Agent, agreed to pay Minatom $84.50/SWU (with escalation according to the U.S Gross National Product Implicit Price Deflator) for the enrichment component of the HEU-derived LEU that it received from Minatom through the end of 2001. This price, which was approximately 12% below the restricted spot market price in November 1996 has escalated to about $88/SWU, 10% above the current spot market price.

In the Fall of 1999, USEC announced that it was considering resigning as the U.S. Executive Agent for the purchase of the Russian HEU-derived SWU unless it received substantial financial support from the government. USEC believed that it should be receiving financial compensation for managing the Russian HEU procurement activities,i.e. a management fee. It claimed that it needed this funding to offset the above market SWU price that it was being forced to pay under the HEU purchase agreement with Minatom. It did not receive any financial support. Although it backed down on its resignation position on December 1, 1999, its actions and attitude caused considerable

concern within both the Administration and the Congress. While it is now committed to be the Executive Agent through the end of the year 2001, it could raise the issue again before the end of this year, though this does not seem likely. The issue of need for government financial support continues to exist.

On June 9, 1999, USEC announced that it was terminating further development of its AVLIS enrichment technology. It was noted that USEC's Board of Directors and management had reached this decision after a comprehensive review of operating and economic factors. USEC's President, William H. Timbers, Jr., stated that USEC had enough data to conclude that the returns would not be sufficient to outweigh the risks and the ongoing capital expenditures necessary to develop and construct an AVLIS plant. USEC's J. William Bennett, Vice President of Advanced Technology stated, as follows:

> *Based on results of a recent series of test runs, we have identified continuing issues that we believe would take at least another year to address satisfactorily and, once addressed, would increase new plant construction costs beyond the previous $2.5 billion estimate. Even if these issues were resolved, the resulting economics, weighed against the market price trends for enrichment, would provide too low a rate of return on investment for the risk involved.*

To many in the industry the AVLIS suspension decision came as a surprise. Secretary of Energy Bill Richardson, in a letter to USEC's William Timbers, said that he was "...surprised that this [suspension] decision would take place so soon after privatization last year. I know there have been changes in the nuclear fuel market, but I understood that USEC considered AVLIS as an asset for its future viability." In its July 29, 1998, Privatization Prospectus, USEC had stated that it planned to complete development and commence commercialization of AVLIS so that it could remain one of the lowest cost suppliers of enrichment services and enhance its competitive position.

As matters now stand, USEC is seeking a promising technology that it can develop as a replacement for its aging GDPs. It is funding an Australian-invented laser technology called Silex that has not yet been proven successful in a laboratory environment. USEC has embarked on a six-month study to evaluate its options for using gas centrifuge, a technology that it does not own and would, therefore, have to acquire from others. It has reportedly had useful discussions with the Department of Energy (DOE) regarding the U.S. centrifuge technology that DOE abandoned in 1985.

Though USEC has apparently also expressed some interest in Russian and Urenco centrifuge technology, it is not known if it has pursued this subject with the Russians and it is understood that it has not done so with Urenco. However, it was reported in the press (NuclearFuel, February 21, 2000), that at a meeting of the German Atomic Forum on February 17, Urenco's Managing Director, Klaus Messer, volunteered that Urenco would be interested in a joint venture with USEC to build and operate a centrifuge plant in the

U.S. Dr. Messer reportedly stated that such an arrangement "would make sense and be logical".
It is Consultant's belief that acquisition of Urenco technology might be possible either through a joint venture such as that suggested by Dr. Messer or through technology acquisition. Technology acquisition could involve purchase of plant and equipment similar to the Chinese purchase of Russian centrifuge technology in the 1990s. Alternatively, acquisition might only involve the purchase of a technology license. It is clear that Dr. Messers' proposed arrangement would likely be the one that Urenco would prefer, especially since it could be structured along the lines of the ill-fated Louisiana Energy Systems (LES) Clairborne plant that was proposed in the 1990s. There might be issues relating to market share that would have to be negotiated.

While the acquisition cost of Russian centrifuge technology might be less than the cost of Urenco technology, this is far from certain. The Russian ability to drive hard bargains has already been demonstrated in the pricing of the HEU deal. It is believed that the overall capital cost of a Russian technology-based plant in the U.S. could be high because of the large amount of piping and related equipment that would be required because of the low output of the individual Russian machines.

3. USEC Financial Status

As USEC's financial troubles became public during the past 18 months, the Wall Street investment community became increasingly concerned about the corporation's diminishing stock value and credit rating. Standard and Poor (S&P) reduced USEC's corporate credit and bank loan rating from BBB+ to BBB on August 30, 1999, one level above S&P's lowest investment grade rating of BBB-. On February 4, 2000, the day following release of USEC's bleak FY 2000 second quarterly report, its S&P credit rating was reduced to BB+, one level below investment grade. On February 23, Moody's also downgraded USEC's credit ratings: its senior unsecured guaranteed bank credit facility was reduced from Baa1 to Baa3, its senior unsecured debentures from Baa1 to Ba1, and its short term debt rating from P-2 to P-3.

S&P and Moody's both stated that "The outlook [for USEC] is negative". Moody's also stated, as follows:

> *Ratings will continue under pressure due to the high cost base relative to SWU prices and the expectation that prices are unlikely to improve from current levels of approximately $80/SWU given overcapacity in the market. While recently announced initiatives concerning employment levels and power costs will provide savings, Moody's expects earnings compression to continue on the present operating profile and market conditions. Additionally, the use of excess cash flow generated to buy back stock will weaken USEC's liquidity position.*

S&P noted that while "USEC's internal cash flow generation remains relatively strong, this largely reflects the planned liquidation of its natural uranium inventories, which will be depleted in 5 to 6 years."

The following table presents USEC's SEC filed condensed statements of income for FY 1998, FY 1999, and the first two quarters of FY 2000.

USEC CONDENSED STATEMENTS OF INCOME
FOR FISCAL YEARS 1998, 1999 AND 2000 (FIRST TWO QUARTERS)

ITEM	FISCAL YEARS ENDED JUNE 30 (Million Dollars) 1998	1999	2000 (2 Qtrs)
Separative Work (SWU) Sales Revenue	1,380.4	1,475.0	637.0
Uranium Sales Revenue	40.8	53.6	41.5
Total Revenue	1,421.2	1,528.6	678.5
Cost of sales	1,062.1	1,182.0	563.8
Gross profit	359.1	346.6	114.7
Special charges:			
AVLIS technology suspension	-	34.7 (a)	-
Workforce reduction & privatization costs	-	46.6	-
Project development costs	136.7	106.4	4.0
Sales, general & administrative	34.7	40.3	23.4
Operating income	141.1	165.2	87.3
Interest expense	-	32.5	18.3
Other (income)	-5.2	-16.8	-5.7
Income before income taxes	146.3	149.5	74.7
Provision (benefit) for income taxes	-	-2.9 (b)	26.0
Net income	146.3	152.4	48.7
Net income per share (basic & diluted) ($)	-	$1.52	0.52
Dividends per share ($)	-	$0.83	0.55
Average number of shares outstanding (million)	-	99.9	94.2

(a) Equivalent to $22.7 million after taxes at the effective rate of 34.5%.
(b) Includes a one-time special income tax benefit of $54.5 million in first six months of FY-1999. Excluding the tax benefit, FY-1999 net income was $40.7 million or $0.41 per share.

The table shows that USEC was able to make the dividend that it promised in its 1998 privatization prospectus, in its first full fiscal year of operation, FY 1999, but with little margin. In its prospectus, USEC noted that it intended to pay annual cash dividends on it outstanding shares at an initial rate of $1.10 per share. The table also presents the company's consolidated statements of income for the first six months of FY 2000, as reported in its Securities and Exchange Commission (SEC) Form 10-Q report that was released on February 3, 2000.

USEC reported earnings for FY 1999 of $120.6 million, or $1.21 per share, excluding a special income tax benefit and special charges related to the suspension of the AVLIS technology program. (This can be estimated from the data in the table, as follows: 152.4 plus 2.9 minus 34.7 = 120.6, all in millions of dollars). Revenue from SWU and uranium sales for the fiscal year totaled $1,528.6 million, compared to $1,421.2 million in the previous year.

Net income for FY 1999 was $152.4 million, which included a special income tax benefit of $54.5 million and special charges of $34.7 million ($22.7 million, or $.23 per share, after tax) for contract terminations, shutdown activities, and employee severance and benefit arrangements related to the termination of AVLIS.

At the time of it privatization in 1998, USEC became subject to federal, state and local income taxes. The provision for income taxes in FY 1999 included a one-time special income tax benefit of $54.5 million for deferred income tax benefits that arise from the transition to taxable status. If the special tax benefit did not exist, then USEC's FY 1999 taxes would have been $51.6 million. Special charges of $34.7 million in FY 1999 are for contract terminations, shutdown activities, and employee severance and benefit arrangements related to AVLIS suspension. Excluding the special income tax benefit would have resulted in a FY 1999 net income of only $0.98 per share. Since all project development costs were charged to expense, there was no asset write-off.

If the first two quarters of FY 2000 are representative of the entire fiscal year, then annual revenues might total $1,357, which is $172 million less than in FY 1999. However, the timing and quantities of SWU contract requirements vary from quarter to quarter and year to year in accord with the refueling schedules of customer's nuclear power plants, and thus, no strong inference can be drawn from the FY 2000 data available so far. While FY 2000 costs do not include the AVLIS costs of the past, revenues are lower due to customer's declining SWU deliveries and declining SWU prices in contract commitments. It is expected that USEC will be able to meet its reduced dividend commitment of $0.55 per share in FY 2000. Based on its first half-year results, USEC has projected a FY 2000 net income at between $110 million and $115 million. As of December 31, 1999, USEC had repurchased 9.62 million shares, and its Board has since authorized the repurchase of a total of 30 million shares of the 100 million shares initially issued.

Revenues in the second quarter of FY 2000 included sales of $42.8 million for temporary replacement of SWU "trapped" at the Tokai Mura accident site in Japan. It is expected that USEC's sales in 2001 and 2002 will be reduced by about this amount as SWU is retrieved from the accident site. While project development costs in the first half of FY 2000 only amounted to $4 million, project development costs are expected to rise to $18 million for the entire year as scheduled payments for Silex, centrifuge research, and other requirements are met.

On February 3, 2000, USEC announced that it expected its FY 2001 net income to be reduced to between $35 million and $45 million, or about one-third of this years expected net income. In its February SEC Form 10-Q report, USEC notes that:

> *Looking ahead to fiscal 2001 and beyond, USEC expects that its financial condition and results of operations will continue to be adversely affected by unfavorable global market conditions for the sale of enriched uranium and the legal constraints placed on USEC's ability to reduce costs in response to these changed market conditions.*

4. Operating Cost Considerations

USEC leases and operates the two DOE GDPs that are located at Paducah, Kentucky and Portsmouth, Ohio. The combined total nameplate capacity of these plants is 18.7 million SWU per year. However, not all of this capacity is economically competitive. As production level increases, the amount of electric power needed to produce an additional SWU increases. Also, after production reaches a certain level, low cost "non-firm" sources of electric power have to be replaced by higher cost "firm" sources of power. The net effect of these operational considerations is that economically competitive production from the two GDPs is limited to between 70% and 75% of nameplate capacity, or 13 to 14 million SWU. Above this level the marginal cost of production rapidly rises from approximately $55 per SWU to well over $100 per SWU. USEC stated in its SEC FY 1998 Form 10-K filing, as follows:

> *At recent electricity rates, average production cost is lowest when the GDPs are operated at a production level of approximately 13 million SWU.*

USEC's purchases of non-firm power have averaged one-third of all power purchases in the past, and were 30% in 1999. Over 50% of the Paducah plant's purchased power is obtained from non-firm sources. Its operations are extremely flexible, allowing it to take advantage of low-cost short-term power opportunities as they arise. Power levels may be changed by 400 MWe on a hour's notice. The non-firm power is purchased directly on a competitive bid basis. However, the USEC's non-firm power rates have been rising recently, although the non-firm percentage of total power purchases is declining as GDP production declines. The USEC's firm contracts for cost-based power supplies run through 2005, and include favorable termination clauses. Total USEC power purchases continue to average about 2.0 cents/kWhe.

Electric power prices at the Paducah plant were unusually high during the 3rd quarter of FY 1998 due to persistent hot weather, high electricity demand in the Midwest, and resulting power generation shortages. USEC was forced to curtail production at Paducah, but earnings for FY 1999 were affected by the record high power costs. USEC limited its exposure to high-cost, non-firm power prices at Paducah for the summer of 1999 by two strategic actions. First, it reduced its power commitments to the Ohio Valley Electric Power Corporation (OVEC) for the Portsmouth plant in return for $31.7 million in cash

payments; USEC referred to this arrangement as "monetizing" excess power available under contract. Second, it made arrangements to move blocks of power from Ohio (Portsmouth location) to the Paducah plant as needed.

Additional important factors affecting USEC's future power costs are industry competition and deregulation, and potential new environmental regulations beyond those already embodied in the Clean Air Act Amendment of 1990 (CAAA). To date, USEC's power suppliers have been able to meet or beat CAAA imposed limits by switching to low-sulfur coal sources, blending low- and high-sulfur coals, and purchasing allowances for SO_2 emissions without major cost increases. USEC power costs have the potential to rise by 5% to 10% through the year 2005. Beyond 2005, however, the costs of potential nitrous oxide (NO_x), particulates, air toxics and even carbon mitigation regulations, could result in real price increases of 2.5% annually. While the timing of such regulations is highly uncertain, even if enacted, they are not expected to affect costs before 2005.

USEC sales are met from two primary sources: (1) production from GDPs and (2) purchases of SWU primarily derived from Russian HEU, but also including a small amount of Russian "matching" SWU purchases and ongoing U.S. HEU-derived SWU transfers. USEC can also meet a small amount of its annual sales from its own enrichment inventories, which include prior transfers of U.S. HEU-derived enrichment from DOE. As USEC's purchased enrichment quantities have increased over the last several years under its agreement to serve as Executive Agent for Russian HEU-derived SWU, the production level of the GDPs has decreased accordingly. As a result, the production requirements of USEC's two GDPs will soon become approximately one-half of former levels, and the impact of the fixed cost components (primarily labor costs) on GDP production costs will increase dramatically.

In the short term USEC can lower its average unit production cost by performing separative work in excess of its contract commitments, and thereby spread its fixed costs over a larger base. This mode of operation, which results in a build up of enriched uranium product inventory, is sometimes referred to as pre-production. USEC can also use excess separative work capacity to underfeed the GDPs. Underfeeding is a process which substitutes increased SWU production and electric power consumption for decreased uranium feed, resulting in an increase in uranium inventories. The specific mode of operation will depend on economic factors such as the price of electricity, the market price of uranium feed, and the cost of tails disposal. It is understood that USEC operated its GDPs in a "net underfed" mode in FY 1998 but not in FY 1999. Net underfed means that that one plant may have been more underfed than the other, depending on the individual economics for each plant.

It is expected that the supply mix to meet projected future USEC annual sales of 11 million SWU per year will be:

GDP Production to Meet Demand	5.0 Million SWU

Russian HEU-derived SWU purchases	5.5 Million SWU
U.S HEU derived SWU purchases	0.5 Million SWU

An additional 0.5 million SWU per year may be used at the GDPs for underfeeding, increasing USEC's stocks of natural uranium by approximately 2 million pounds per year. USEC may also decide to draw down its existing SWU inventories in the future.

The following table presents the composition of USEC's current and historic GDP production costs, total GDP production cost, annual GDP production, average sales price, and SWU purchases. These figures are derived from the USEC privatization prospectus and SEC filings.

USEC GDP PRODUCTION COSTS

USEC Fiscal Year:	1995	1996	1997	1998	1999
Components of Production Cost ($/SWU and Percent of Total)					
Electric Power	$43.2	$46.0	$51.3	$45.5	$50.5
	57%	55%	59%	48%	56%
Labor and Benefits	$15.4	$20.4	$22.1	$30.5	$27.7
	20%	24%	25%	32%	31%
Tails Disposition	$9.0	$8.8	$6.9	$7.1	$4.7
	12%	10%	8%	8%	5%
Other	$7.6	$9.0	$7.1	$10.7	$7.4
	10%	11%	8%	11%	8%
GDP Production Cost ($/SWU) *	$75.2	$84.1	$87.5	$93.8	$90.3
	100%	100%	100%	100%	100%
GDP Production (Million SWU) **	13.6	10.6	10.3	8.9	8.6
Average USEC Sales Price ($/SWU)	$116.4	$118.4	$114.9	$116.0	$115.2
USEC Purchases (Million SWU)	1.2	2.0	3.1	5.3	3.9

Totals may not add due to rounding
* Transaction tails basis.
** Operating tails basis.

As demonstrated in the above table, as SWU purchases increase and SWU production decreases, the labor and benefits share of total unit production cost rises --- an 80%

increase since FY 1995. Not surprisingly, GDP production costs have also risen. Tails expenses have dropped due to the use of lower estimates of the future unit cost of tails disposition and use of underfeeding, which decreases tails production. It is clear that further reductions in labor costs will be required if GDP production is to be profitable at expected future production levels.

At the present time, USEC is able to earn a profit since the average sales price for deliveries made during FY 1999 was $115 per SWU (as reported by USEC). The FY 1999 sales price includes older contract commitments with higher prices. It is observed from the above table that GDP production costs have risen to a level consistent with or higher than industry-wide new sales contract pricing for delivery in future years (mid $80s per SWU). As more recently signed contracts begin to constitute a larger percentage of USEC deliveries, it is expected that average prices received by USEC will drop to levels at or even below the FY 1999 GDP production cost.

USEC acknowledged the trend toward lower SWU pricing in its June 1998 prospectus for the initial public offer. It apparently hoped to combat the obvious negative effect on profitability by lowering GDP production costs, deploying a lower-cost AVLIS technology, and increasing absolute sales levels. Although USEC has maintained its average sales levels at approximately 12 million SWU per year during the past few years, its FY 1999 world market share is about 35%, down from the 40% level that it had in FY 1997. Its FY 2000 market share is expected to decline to about 32%.

The other major component of USEC supply is provided by the purchase of HEU-derived SWU supplies from Russia at $84.50 per SWU plus inflation from 1997. USEC also incurs shipping costs estimated to be about $2 per SWU. The total cost for USEC of Russian HEU-derived SWU purchases made in FY 1999, was approximately $90 per SWU. Clearly, the Russian HEU-derived supply suffers from the same problem as GDP production, a cost that is above the current market price for new long-term enrichment contracts. The Russian HEU pricing applies for deliveries through the end of calendar year 2001. Negotiations for a delivery schedule and prices in 2002 and beyond are already underway.

In addition to covering its production costs, USEC must generate sufficient operating revenues to provide for general, selling and administrative (GS&A) costs, interest costs, R&D cost ($100 million in FY 1999; only $18 million scheduled for FY 2000), and income taxes and still have enough left to pay dividend distributions to stockholders. Based on an analysis of published USEC costs for FY 1998 and FY 1999, the margin necessary to generate the $1.10 dividend payments promised in the prospectus, as well as the other non-production costs just listed, would amount to an additional $18 to $20 per SWU.

While profit expectations may have been met by USEC at the average SWU delivery price of $115 per SWU during FY 1999, the situation is expected to change rapidly for USEC as

future delivered prices drop in real terms and GDP unit operating costs continue to increase. In the future, USEC uranium inventory sales, which are discussed separately below, and sales of lower cost U.S. HEU-derived SWU inventories can be expected to provide approximately $4 per SWU in after tax profits to compensate in part for lack of profits from sales of enrichment services. Up to $2 per SWU in additional savings may be generated by USEC efforts to limit exposure to high-cost, non-firm power during the summer, monetize excess summer power available under one power contract, and wheel blocks of lower-cost power from one GDP to the other when needed.

5. USEC's Market Position

In its Form 10-K filing with the SEC for FY 1999, USEC claimed a world enrichment market share of 35% and a North American (the U.S. and Mexico) market share of 73%. These market shares make USEC the number one supplier of commercial enrichment services to electric utilities in both the U.S. and the world, with total commercial sales 50% higher than the next largest Western world supplier. USEC's customer backlog through 2010 is approximately $7.2 billion, in escalated dollars.

USEC's domestic market share for enrichment services has gradually declined since 1990, a point in time when its DOE predecessor held 90% of the U.S. market, to its current (2000) level of about 65%. The U.S. market share is expected to decline to between 60% and 65% during the next few years based on current contract commitments. The decline in U.S. market share is the natural result of greater competition and customer preference for diversity among its suppliers. Thus far, the decline in USEC's U.S. market share has been partially offset by an increase in overall U.S. requirements for uranium enrichment services, which has resulted from improved nuclear power plant operating performance.

USEC's share of the world enrichment services market is also expected to decline by about 10% during the next several years. The other major world markets for enrichment services are the Far East and Europe. USEC and its predecessors have historically been the dominant supplier in the Far East, where indigenous supply capacity is small. USEC's current market share for the Far East is estimated to be 52%, from which USEC generated 30% of its 1999 sales revenue. USEC's current share of the European market is relatively small (~6%). This is due largely to the domination of the European markets by indigenous suppliers Eurodif and Urenco. The European market generated about 8% of USEC's 1999 sales revenue.

6. USEC's Marketing Strategy and Behavior to Date

USEC's marketing strategy, both as a private company and as a wholly- owned government corporation, appears to have been based on maintaining or increasing its market share. A strong market share appears to have been viewed by USEC management as crucial to its successfully completing the privatization process. During the early 1990s, the government corporation offered discounts on existing contract commitments in

exchange for additional new sales commitments at prevailing market prices. As European competitors sought to gain a strategic foothold in the U.S. market, the price for enrichment services under long-term contracts began to drop. At that time, USEC appeared unwilling to accept any loss in market share, and continued to lower its price offerings on subsequent proposals following a competitive bidding loss. After the Western European competitors satisfied their U.S. market share goals of 10% to 15% each, they became less active in the U.S. market, but USEC did not seem to readjust its strategy. It continued to submit low price offers in its proposals and win the vast majority of subsequent new contracts at unnecessarily low prices. As the European competitors re-entered the U.S. market, in order to maintain their previous market share gains, both the market price and USEC's offering prices declined once again. However, financially weakened by its growing obligations to deliver significant quantities of future enrichment services at very low prices, USEC may have finally decided to refocus its marketing strategy.

In its SEC Form 10-Q report for the quarter ending March 31, 1999, USEC stated that it:

> *"has resisted lowering prices to levels that would fail to meet its margin requirement even when it has meant a decline in market share. USEC's focus is on profitability rather than market share."*

However, it is not clear what USEC's definition is of its "margin requirement". If it is based on the average cost of sales, including fixed cost components such as labor and depreciation, then USEC has been competing at prices that are below current costs and thus do not afford a profit margin. In making the above statement, USEC may have been assuming significant reductions in its future costs.

USEC also recognized the low price levels for new long term contracts and listed contributing factors when it stated:

> *Recent industry and global economic developments have intensified the effects of production over-capacity and continuing lower prices for enrichment services. These developments include: the adverse impact of the strengthening U.S. dollar; recent decisions by certain European utilities to liquidate strategic SWU inventories; termination of the Kazakhstan suspension agreement; a reduction in the open global demand for SWU; and heightened price competition among uranium enrichment suppliers.*

Prices for new long term enrichment contracts have fallen steadily over the past six years, from approximately $100 per SWU in 1994, to the mid $90s per SWU in 1996, and the low $80s per SWU by 1999, all in then-current dollars. The spot market enrichment market price decline leveled off during the past six months at about $80 per SWU, with the long term price being only a few dollars higher. Prices could rise during the next few years to the low $90s per SWU in response to some expected modest increase in world

requirements, the possible shutting down of excess USEC production capacity, potential weakening of the U.S. dollar, and less intensive competition among suppliers.

7. Uranium Inventories

At the time of its privatization in July 1998, USEC reported its inventories as totaling 74.755 million pounds uranium equivalent (U_3O_8e). The inventories were composed of material already owned by USEC, transfers made by DOE between March 1998 and July 1998, and HEU-derived LEU that is committed to be transferred by DOE after blending has been completed. A breakdown of the inventories, in million pounds U_3O_8e, is as follows:

Inventories held on March 31, 1998	31.73
7,000 MTU natural UF_6 in accord with 1996 Privatization Act	18.29
50 MT HEU in accord with 1996 Privatization Act	13.07
3,800 MTU as UF_6 remedial action payment by DOE	9.93
45 MTU LEU remedial action payment by DOE	1.18
0.8 MT HEU remedial action payment by DOE	0.55
Total:	74.75

The 7,000 metric tons of uranium (MTU) and 50 MT HEU uranium, corresponding to 31.36 (=18.29+13.07) million pounds U_3O_8e, is restricted from being sold into the U.S market at a rate that is greater than 10% per year, that is, at greater than 3.14 million pounds per year. The 3,800 MTU and the 45 MTU LEU (corresponding to a total of 11.11 (=9.93+1.18) million pounds U_3O_8e) is restricted from being sold into the U.S. market at a rate that is greater than 35% per year, that is, at a rate that is greater than 3.89 million pounds per year. The total must be sold over at least four years. The remaining material is unrestricted.

In addition to its inventories, as previously stated, USEC underfed its GDPs in FY 1998 but not in FY 1999. Underfeeding may have "generated" as much as four million pounds of uranium equivalent (U_3O_8e) in FY 1998. However, since the approximately 75 million pound inventory noted above is for the end of the third quarter of FY 1998, it is estimated that the March 31 inventory was only increased by about one million pounds by the time of privatization. It is estimated that USEC could in the future potentially accumulate up to about 2 million pounds U_3O_8e per year through underfeeding, that is, by operating its enrichment plants at 0.26 weight percent (w/o) U-235 while transacting with customers at 0.30 w/o, depending on the economic justification at the time.

USEC's SEC filings indicate that its revenues for uranium sold in FY 1999 and the first half of FY 2000 were $53.6 million and $41.5 million, respectively. It can be estimated on the basis of spot market prices during these two periods that these sales depleted USEC's uranium inventory by about 8 million pounds U_3O_8e, leaving it with an end of calendar year 1999 inventory of approximately 68 million pounds U_3O_8. However, according to reports (e.g. NuclearFuel, July 13, 1998) USEC had already committed about two million pounds U_3O_8e per year through 2005 when it was privatized in mid-1998, and

was committed to deliver approximately 12 million pounds between the end of 1999 and the end of 2005. If USEC has since doubled its commitment for this period as a result of sales made between mid-1998 and the end of 1999, then its end of 1999 uncommitted inventory would have been approximately 44 million pounds. If USEC's January 2000 commitment to the Tennessee Valley Authority (TVA) is included, between 15 and 20 million pounds over ten years, then USEC's uncommitted inventory currently amounts to between 24 and 29 million pounds. In its 1998 privatization prospectus, USEC stated that it would withhold 13 million pounds for GDP operational requirements --- this is equivalent to about three months of working inventory. Since the purchase of HEU-derived SWU will result in a GDP annual production level of only about 5 million SWU, a working inventory of 6 million pounds U_3O_8e should be adequate. This means that USEC's uncommitted uranium inventory could currently be between about 18 and 23 million pounds. Because the foregoing is based on best estimates, it would be conservative to assume that USEC's forward uranium sales from existing inventory will be limited to a total of 20 to 30 million pounds. Uranium accumulated from underfeeding could increase these quantities by about two million pounds per year.

Consultant estimates that USEC's delivery commitments will range between 6 and 8 million pounds per year through the middle of this decade and then taper off by 2010. However an additional 2 million pounds per year may be obtained through underfeeding, if economically justifiable, in which case sales may be accordingly higher. USEC's uranium sales, already largely committed as shown above, could generate revenues of approximately $81 million per year. This is based on annual sales of 2.7 million kilograms (7 million pounds) of uranium hexafluoride (UF_6) at $30 per kilograms of uranium(as UF_6). However, it should be recognized that while this would generate cash flow, the uranium has an underlying cost that is about 75% of the estimated market value, that is, $22.50 per kilogram. The underlying cost was estimated as being between $20 and $25 per kilogram, based on information given in USEC's 1998 Privatization Prospectus. Using an effective federal and state income tax rate of 34.5%, the resulting contribution to after tax profit from the sale of the uranium inventory may be estimated as being as little as 16% of the cash generated or about $13 million per year. This would correspond to a benefit of about $1.20 per SWU on annual sales of 11 million SWU.

8. Strategies for the Future

Over the past six months, USEC has effectively signaled that its strategy for future viability is going to be based on:

- Shutting down portions of excess capacity at both of its GDPs or completely shut down one of the two plants;
- Negotiating a substantial price reduction in the HEU-derived enrichment purchased from Russia and/or obtain "peace dividend" compensation from the U.S. government;
- Reducing its workforce to the minimum level necessary to continue safe operation of the GDP(s); and

- Acquiring access to centrifuge technology to replace its diffusion technology as soon as feasible.

None of these plans are a great surprise to industry observers, and all make good business sense. If they can be completed successfully and market prices rise into the low $90s per SWU, then USEC should be able to maintain some level of profitability. USEC now operates as a commercial business, and must meet its fiduciary responsibilities to stockholders. While USEC's fortunes can be strongly affected by U.S. government policies, USEC cannot set those policies, rather, it can only react to them in the most business-like way possible.

USEC is somewhat limited in its options to rationalize excess production capacity due to one of the conditions agreed upon as part of privatization, namely that both GDPs be kept running until 2005 unless one of a number of criteria indicative of poor financial performance are triggered. The 1998 agreement between USEC and the Treasury Department requires that USEC operate the two GDPs until the end of 2004, subject to the following exceptions:

- The occurrence of any event beyond the reasonable control of USEC, such as fires, floods, or acts of God, that prevent continued operation of the plants;
- If the Operating Margin (earnings plus interest and taxes divided by total revenue) of USEC is less than 10% in a twelve consecutive month period;
- If the long term credit rating of USEC is, or is reasonably expected in the next twelve months to be , downgraded below an investment grade rating;
- If the Operating Interest Coverage Ratio (earnings plus interest plus taxes divided by gross interest expense) of USEC is less than 2.5 in a twelve consecutive month period;
- If there is a decrease in annual worldwide demand for SWU to less than 28 million SWU; or
- If there is a decrease in the average price for long-term firm contract delivery of SWU to less than $80 per SWU, in 1998 dollars.

While some of these criteria are not very precisely defined, and are, therefore, subject to interpretation, the recent S&P and Moody's down downgrading has clearly triggered one of the criteria and put USEC in a position to begin planning a plant shutdown. In addition, there could be a decline in the Operating Margin in the next year or two that could provide a second shutdown trigger opportunity for the corporation. The table below presents consultant's estimates of the actual Operating Margins for FY 1998 and FY 1999, and projected Operating Margins for FY 2000 and FY 2001. It is projected that the Operating Margin could decline to about 7.7% in FY 2001, that is, by the end of calendar year 2000.

USEC OPERATING MARGIN

	← Actual		Projected →	
	FY 98	FY 99	FY 00	FY 01
SWU Sold (Millions)	11.9	12.8	12.0	11.0
Avg. Price ($/SWU)	$116.0	$115.0	$111.4	$106.1
GDP Production SWU (at trans. Tails)	7.8	8.6	6.0	5.0
GDP Production Cost ($/SWU)	$93.8	$90.3	$101.7	$103.2
Net Profit (Million $)	$146.3	$152.4	$94.9	$45.9
Operating Margin	13.2%	13.1%	12.1%	7.7%

Despite the AVLIS program termination, USEC contends that it is still pursuing options to secure a cost-effective advanced enrichment technology:

> *We are moving forward with our evaluation of potentially more economical technology options, including the Silex laser enrichment process and gas centrifuge technology." ... "USEC has secured exclusive rights to explore the commercial viability of the Silex enrichment process.*

The separation of isotopes by laser excitation, referred to as Silex, is under research and development (R&D) by the Australian company, Silex Systems Limited (SSL), at the Australian government's atomic energy facilities at Lucas Heights, New South Wales, Australia. The research, still at the laboratory stage, reportedly resulted in demonstration of key physics parameters by the end of 1999. USEC is continuing to fund the program through mid-2000.

The Silex process has not been publicly described, but is believed to be generally similar to the molecular laser isotope separation (MLIS) process that was researched and eventually abandoned in the U.S., South Africa, Germany and Japan. The research in these countries was abandoned because of the projected poor economics of the relatively low mass efficiency process. Because of restrictions imposed by the Australian government, Silex could not be used to produce HEU fuel for the U.S. Navy, something that could become necessary at some time in the future if USEC were to use only Silex for enrichment in the U.S.

USEC has had discussions with DOE regarding the centrifuge technology that DOE abandoned in 1985. It has also expressed interest in Russian and Urenco centrifuge technology. Unless it obtains centrifuge technology through either licensing or merger-acquisition arrangements with others, it will have to pursue a long and slow R&D path, one that could take a great many years before providing a return. With regard to mergers

and acquisitions, it should be noted that foreign entities are currently prohibited from collectively having ownership of more than 10% of USEC's voting securities. Entities having a significant commercial relationship with a foreign enricher, as well as foreign enrichers and their affiliates, are also currently prohibited from owning any securities of USEC's. It may require legislation to relax the existing foreign constraints.

9. Conclusions

USEC's strategy of maintaining market share "at any cost" has not worked and must now be revised. While there are indications that marketing revisions are underway, it could be a year or more before a revised strategy is complete and an improved outlook for USEC is apparent. In the meantime USEC must resolve the issues of plant shutdown and production costs, the pricing of Russian HEU-derived SWU, and advanced technology for future deployment.

During the next one to two years there is some likelihood that USEC may be regarded as a takeover target by other companies in the industry and by venture capitalists, particularly if its share price remains as low as it is currently. Any takeover is subject to the constraint that no entity can acquire more than 10% of USEC's voting securities for a three-year period following privatization. However, there are indications that the Congress may be willing to reduce the three-year limit.

By the end of next year, USEC must, and probably will, seek to obtain a substantial reduction in the price it must pay for the SWU component of the Russian HEU-derived low enriched uranium. The corporation, reasonably, maintains that the current price is far too high for it to bear, when compared to its own marginal cost of production. The Administration may be able to assist USEC in convincing the Russians of the wisdom of tying price to prevailing market prices, and at some reasonable discount because of the annual volume of SWU involved and the long term of the agreement.

In order for USEC's financial viability to be restored as soon as possible, it must reduce costs substantially since it will not be possible to increase the revenues that are projected to result from the contracts in its current portfolio. The shutdown of one of the GDPs is an unavoidable necessity in this regard, if the company's viability is to be assured. Substantial cost reductions could result from a reduction in the GDP operating labor force from over 3,000 to about 1,500 workers. While the impact on labor would be significant, the DOE may be able to offer alternative employment in some of its remedial action programs.

For the mid to longer term, USEC must identify a reasonable cost centrifuge replacement technology for its aging GDPs. This will require an evaluation of all of the realistic options that may be available, ranging from arrangements that may involve corporate mergers to acquiring technology through licensing agreements. While Silex could turn out to be a commercially deployable technology someday, it will be some years before USEC can rely on this becoming a possibility. In the meantime it must look to proven economic technology to meet its needs.

DEPARTMENT OF THE TREASURY
WASHINGTON, D.C.

July 22, 1998

CLOSE HOLD

ASSISTANT SECRETARY

MEMORANDUM FOR SECRETARY RUBIN
DEPUTY SECRETARY SUMMERS

THROUGH: John D. Hawke, Jr.
Under Secretary
(Domestic Finance)

FROM: Gary Gensler
Assistant Secretary
(Financial Markets)

SUBJECT: Sale of the United States Enrichment Corporation

ACTION FORCING EVENT:

On June 24, 1998, you delegated to Under Secretary John D. Hawke, Jr. the authority of the Secretary under legislation authorizing the privatization of the United States Enrichment Corporation ("USEC" or the "Corporation").

Under Secretary Hawke redelegated such authority to Assistant Secretary Gary Gensler. On June 28, 1998, Assistant Secretary Gensler conditionally approved on your behalf the decision of the Board of Directors (the "USEC Board") of USEC to privatize the Corporation through an initial public offering (the "Offering"), subject to further determinations by the USEC Board and Treasury that no event or condition has occurred since the date of the conditional approval that would cause a change in the assessment that the Offering satisfies the statutory requirements for privatization. On June 29, 1998, USEC filed a registration statement with the Securities and Exchange Commission and initiated a road show for the sale of the common stock of the privatized corporation. The USEC Board will meet this afternoon and we expect them to make its required determination that the Offering continues to satisfy the statutory requirements for privatization. After the close of the securities market this afternoon, we expect the underwriters to offer to purchase from the Treasury 100% of the common stock at a price. The filing range was between $13.50 and $16.50 per share. We understand that the current expected price is approximately $14 per share. Assistant Secretary Gensler intends to give final approval to the sale based on our belief that no event or condition has occurred since June 28, 1998, that would cause a change in the assessment that the Offering satisfies the statutory requirements set forth by Congress.

RECOMMENDATION:

That you determine that the actions that Assistant Secretary Gensler intends to take in giving final approval to the sale through the Offering are consistent with your delegation of authority.

DECISION:

✓ Approve _____ Disapprove _____ Let's Discuss

DISCUSSION:

We believe that no event or condition has occurred since June 28, 1998, that would cause us to change our assessment that the Offering satisfies the statutory requirements for privatization. The more significant recent issues that have been addressed in considering the privatization are set forth below:

Proceeds:

We anticipate that after the close of the public securities market, Morgan Stanley and Merrill Lynch, the co-managers, will inform us that the underwriters are prepared to purchase 100 million shares of USEC Inc. We understand that the underwriters currently expect that they will price the shares at approximately $14 per share. Accordingly, the proceeds from the sale of these shares will be approximately $1.4 billion, less the underwriting discount of 2.96%. USEC will also obtain debt financing of $500 million to pay to the Treasury as an exit divided. The combined proceeds from the Offering and the debt financing will result in aggregate proceeds to the United States of approximately $1.9 billion, less the discount.

You may recall that the Carlyle Consortium offered $1.9 billion, with $100 million of such proceeds set aside in an indemnification escrow account for up to six years and post closing adjustment for tax basis.

Effects on the Communities:

The Offering is likely to result in the reduction of 600 jobs, 100 jobs through attrition, at the gaseous diffusion plants operated by USEC in Paducah, Kentucky and Portsmouth, Ohio over the next two fiscal years. USEC has entered into two agreements with the Department of Energy ("DOE") to ameliorate the effect of staff reductions. Under the first agreement, DOE will assume responsibility for a certain amount of depleted UF_6 generated by the privatized company for a payment of $50 million from USEC's pre-privatization funds. DOE will apply these funds through its "work for others" program for two purposes. First, DOE will initiate research and development for the establishment of a facility to treat the depleted uranium. If constructed, the new facility would create a significant number of jobs. Second, DOE will establish a canister maintenance program to enhance the protection of the depleted uranium. DOE has stated its intention to give hiring preferences under its canister maintenance program to qualified USEC workers that are affected by the staff reductions. Under the second agreement to ameliorate the effect of job reductions, USEC is providing certain worker transition assistance benefits using $20 million from USEC's pre-privatization funds.

The disposition of depleted uranium is also addressed by legislation unanimously adopted by the Senate on July 16, 1998, and adopted by the House on July 20, 1998. We expect that the legislation will be signed into law prior to the closing date. The legislation will set aside approximately $385 million from USEC's revenue account and will direct DOE to prepare, by fiscal year 2000, a plan for applying these funds to the disposal of depleted uranium and the construction of onsite disposal facilities at each of the gaseous diffusion plants operated by USEC.

On June 27, 1998, USEC entered into a letter agreement with Treasury in which it agreed that, in the event of the Offering, it would contractually commit to operate the gaseous diffusion plants until January 1, 2005, unless a significant event occurs that could threaten USEC's viability or the maintenance of a reliable domestic enrichment industry. By a letter to Treasury dated July 10, 1998, USEC clarified some of the exceptions to its obligation to operate the plants, and provided assurance that current projections do not anticipate the occurrence of events that would allow plant closings under these exceptions. These clarifications were incorporated into an agreement signed on July 14, 1998.

National Security:

Subsequent to our June 28, 1998, decision to proceed with the Offering, the Administration has received a number of expressions of concern regarding national security aspects of the privatization: first, the effect of USEC's projected uranium sales on the agreement now being negotiated between Russia and western companies to sell Russia's natural uranium; and second, USEC's commercial interests may be in conflict with its role as Executive Agent under the Russian HEU Agreement. These issues have been discussed by the interagency groups since the initiation of the privatization process in 1995. In response to heightened concern with these issues, consultations took place over the last month among senior officials of Treasury, the Office of the Vice President, the National Security Council, the Council of Economic Advisers, the National Economic Council, the Department of State ("DOS"), DOE, and the Office of Management and Budget. On July 20, 1998, senior Administration officials met with Senator Domenici to discuss these issues. Additionally, USEC provided DOS with written clarifications on July 21, 1998, providing a comprehensive summary of its policies and plans with respect to completed sales of natural uranium, an elaboration of its statements made in the Registration Statement of its intent to sell natural uranium, and its viels on the importance of remaining in the Executive Agent for the Russian HEU Agreement. We understand that on July 22, 1998, Samuel R. Berger, Assistant to the President for National Security Affairs, advised President Clinton that, notwithstanding the national security issues raised, the privatization of USEC should proceed. Additionally, DOS has informed us that it concurs with Mr. Berger.

Dual Path

The decision on June 28, 1998, to privatize USEC through an initial public offering was based on an analysis of privatization alternatives and a determination that the Offering was superior to the leading negotiated sale proposal made by the Carlyle Consortium. On July 16, 1998, the Carlyle Consortium modified its offer to incorporate certain provisions of an agreement between USEC and Treasury that limit workforce reductions at the gaseous diffusion plants. Notwithstanding this modification, we have not undertaken a new "dual path" decision as there remain significant differences between the Carlyle Consortium proposal and the Offering as set forth in our memorandum to you, dated June 24, 1998.

DEPARTMENT OF THE TREASURY
WASHINGTON, D.C. 20220

July 22, 1998

MEMORANDUM FOR GARY GENSLER
Assistant Secretary
(Financial Markets)

FROM: Peter C. Necheles
Senior Advisor
(Government Financial Policy)

Roberta K. McInerney
Assistant General Counsel
(Banking and Finance)

SUBJECT: Treasury Approval of the Privatization of the United States Enrichment Corporation through an Initial Public Offering

ACTION FORCING EVENT:

On June 28, 1998, on behalf of the Secretary of the Treasury (the "Secretary"), you conditionally approved the June 11, 1998, decision of the Board of Directors (the "Board") of the United States Enrichment Corporation ("USEC" or the "Corporation") to privatize USEC through an initial public offering (the "Offering") and made a related determination regarding the proceeds of the Offering to the Treasury.[1]

Your conditional approvals and determination were subject to: (1) a further determination by the Board, immediately prior to the execution of an underwriting agreement in connection with the Offering (the "Underwriting Agreement"),[2] that no event or condition has occurred since June 11, 1998, that would cause the Board to change its assessment that the Offering satisfies the statutory requirements set forth in the Atomic Energy Act of 1954, as amended by the Energy Policy Act of 1992,[3] and the USEC Privatization Act[4] (collectively, the "Privatization Legislation"); and (2) a further determination by the Secretary, immediately prior to the execution of the Underwriting Agreement, that no event or condition has occurred since June 28, 1998, that would cause the

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[1] Exhibit 1. Decision memorandum on the privatization of the United States Enrichment Corporation, dated June 28, 1998 (the "June Memorandum"). Capitalized terms used herein and not defined shall have the meanings given such terms in the June Memorandum.

[2] Exhibit 2. Underwriting Agreement dated July 22, 1998.

[3] Pub. L. No. 102-486, 106 Stat. 2776 (1992), 42 U.S.C. 2297 et seq.

[4] Pub. L. No. 104-134, 100 Stat. 1321 (1996), 42 U.S.C. 2297h et seq.

Secretary to change his assessment that the Offering satisfies the statutory requirements set forth in the Privatization Legislation. In order for the Offering to proceed, the Secretary must make such a determination and execute the Underwriting Agreement. The order and directive delegating to you the authority of the Secretary under the Privatization Legislation remain in effect.[5]

Since your approval, USEC has filed a registration statement with the Securities and Exchange Commission and an amendment thereto.[6] Additionally, the Board has made the required determination as described above.[7] The underwriters have now offered to purchase from the Department of the Treasury ("Treasury") 100% of the common stock of USEC Inc.[8] at $14.25 per share.

RECOMMENDATION:

For the reasons discussed in this memorandum and the June Memorandum, we recommend that you, on behalf of the Secretary, make the determination set forth below, sign the attached letter (Attachment A) communicating to USEC this determination, execute and deliver the Underwriting Agreement attached hereto (Attachment B), and execute and deliver such other documents as may be necessary or appropriate to allow the consummation of the Offering.

DETERMINATION:

No event or condition has occurred since June 28, 1998, to have caused the Secretary to change his assessment that the Offering satisfies the statutory requirements set forth in the Privatization Legislation.

_____ Approve _____ Disapprove _____ Let's discuss

DISCUSSION:

In the June Memorandum we described the process followed by USEC, the Treasury, and other relevant agencies, and the specific statutory criteria set forth in the Privatization Legislation. We

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[5] Exhibit 3. Order from Secretary Rubin delegating to Under Secretary Hawke the Secretary's authority to exercise any right or power, make any finding or determination, or perform any duty or obligation which the Secretary is authorized to exercise, make or perform pursuant to the legislation authorizing the privatization of USEC. Redelegation of such authority from Under Secretary Hawke to Assistant Secretary Gensler.

[6] Exhibit 4. Registration Statement, dated June 29, 1998, and Amendment No. 1, dated July 20, 1998.

[7] Exhibit 5. Board Resolution Approving the Offering, dated July 22, 1998.

[8] The holding company of USEC's successor entity after giving effect to the privatization.

analyzed the evidence supporting the Board's conclusion that the Offering will satisfy the statutory criteria and concluded that the Board's decision was made in accordance with the requirements of the Privatization Legislation. Additionally, we analyzed the information made available to us from the Corporation, the Board, the privatization advisors,[9] relevant federal agencies, and the leading candidate for a negotiated third-party sale, and, in considering the options for privatization, concluded that the Offering is superior in accomplishing the objectives of the Privatization Legislation. Based on the analysis that follows, we believe that no event or condition has occurred since the approvals and determination made by you on June 28, 1998, that would cause the Secretary to change his assessment of the satisfaction by the Offering of the statutory requirements set forth in the Privatization Legislation.

On July 16, 1998, Treasury received a letter from the Carlyle Consortium extending the date of its offer for the acquisition of USEC to July 31, 1998.[10] Additionally, the Carlyle Consortium modified its offer to incorporate certain provisions of an agreement between USEC and Treasury that limit workforce reductions at the gaseous diffusion plants. Notwithstanding this modification, we have not undertaken a new "dual path" decision as there remain significant differences between the Carlyle Consortium proposal and the Offering as set forth in the June Memorandum. Additionally, on July 17, 1998, Treasury received a letter from the Texas Pacific Group Consortium expressing its continued interest in acquiring USEC.[11]

In connection with the Offering, USEC has established several wholly-owned subsidiaries. Through a series of mergers that will occur immediately prior to the closing of the Offering, ownership of the assets and obligations of USEC will be transferred to a Delaware-chartered corporation, which will become a wholly owned subsidiary of USEC Inc., the corporation whose common stock will be sold in the Offering. Simultaneously with the closing of the Offering, USEC Inc. will obtain a $700 million credit facility from the Bank of America National Trust and Savings Association. At closing, USEC Inc. will borrow $550 million under the credit facility, of which $500 million will be paid to the Treasury (the proceeds paid to the Treasury are referred to as the "Debt Proceeds").

In discussions earlier today with the co-lead managers of the Offering, Morgan Stanley and Merrill Lynch, we were provided with access to the underwriters' book of orders and, in coordination with the Board, we discussed the price for the Offering. Based upon such discussions, the underwriters agreed to price the common stock of USEC Inc. at $14.25 per

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[9] To assist in the privatization, USEC retained the services of Morgan Stanley & Co. ("Morgan Stanley"), as transaction manager and co-lead manager, Merrill Lynch & Co. ("Merrill Lynch"), as co-lead manager, J.P. Morgan & Co. Incorporated ("J.P. Morgan"), as financial advisor, and Skadden, Arps, Slate, Meagher & Flom LLP ("Skadden Arps") (collectively, the "privatization advisors").

[10] Exhibit 6. Carlyle Consortium letter, dated July 16, 1998.

[11] Exhibit 7. Texas Pacific Group Consortium letter dated July 17, 1998.

share. Thus, the Offering and Debt Proceeds will result in aggregate gross proceeds to the federal government from the privatization of $1.925 billion.

This afternoon we were informed by the Chairman of the Board that it authorized the Offering of 100 million shares of the common stock of USEC Inc. at a price of $14.25 per share. The Chairman also informed us that the Board provided final approval to the privatization by determining that no event or condition has occurred since June 11, 1998, that causes the Board to change its assessment that the Offering satisfies the statutory requirements for privatization set forth in the Privatization Legislation. In discussions today, we confirmed that no event or condition has occurred since June 28, 1998, that causes the Departments of Energy ("DOE"), the Office of Management and Budget ("OMB"), or the Nuclear Regulatory Commission ("NRC") to modify their earlier advice to Treasury that the Offering complies with the Privatization Legislation.[12]

Requirements of the Atomic Energy Act of 1954, as amended by the Energy Policy Act of 1992

Under the Atomic Energy Act of 1954, as amended, the Board is required to determine, in consultation with appropriate agencies, that privatization will satisfy the following criteria:

(1) **Privatization through the Offering will result in a return to the United States at least equal to the net present value of the Corporation.**

As discussed in the June Memorandum, a number of studies conducted by USEC, its financial advisors and Treasury examined the net present value of USEC if it were to continue to operate as a government corporation, pursuant to its current authorities. The resulting valuations range from $100 million to $1.08 billion. The most recent analysis concluded that the net present value of the in-government case ranges from $675 million to $762 million.

Morgan Stanley and Merrill Lynch have informed us that the underwriters are prepared to purchase 100 million shares of USEC Inc. for $14.25 per share pursuant to the Underwriting Agreement. Accordingly, the proceeds from the sale of these shares will be $1.425 billion, less the underwriting discount of approximately $42 million and the success fee for J.P. Morgan of $6.75 million, resulting in net Offering proceeds of approximately $ 1.375 billion.[13] Combined with the net Debt Proceeds, the aggregate net proceeds to the federal government will be

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[12] On July 20, 1998, you consulted with Betsy Moler, Acting Secretary of DOE, and Jack Lew, Acting Director of OMB, who confirmed the continued support of their respective agencies for the privatization of USEC through the Offering.

[13] Privatization expenses, except for the underwriting discount, will be paid from USEC's revenue account at the Treasury. As an asset of the federal government, the revenue account consists of government funds that, to the extent not needed for privatization expenses, will be transferred to the Treasury general fund. Because the balance of the revenue account has already been recorded as receipts by the federal government, the funds in such account are not included in the proceeds of the privatization.

approximately $1.875 billion. This amount exceeds the highest of the net present valuations of USEC if it were to continue to operate as a government corporation.

Accordingly, to our knowledge, no event or condition has occurred since June 28, 1998, that would cause us to change our assessment that the Board's conclusion that privatization through the Offering will result in a return to the United States at least equal to the net present value of the Corporation, is supported by the evidence and in accordance with the requirements of the Atomic Energy Act of 1954, as amended.

(2) **Privatization through the Offering will not result in the Corporation being owned, controlled, or dominated by an alien, a foreign corporation, or a foreign government.**

We have reviewed the certificate of incorporation for each of the Delaware corporations being formed in connection with the privatization,[14] and have confirmed that each such document includes the restrictions on foreign ownership and control described in the June Memorandum. To our knowledge, no event or condition has occurred since June 28, 1998, that would cause us to change our assessment that the Board's conclusion that privatization through the Offering will not result in the Corporation being owned, controlled, or dominated by an alien, a foreign corporation, or a foreign government, is supported by the evidence and in accordance with the requirements of the Atomic Energy Act of 1954, as amended.

(3) **Privatization through the Offering will not be inimical to the health and safety of the public or the common defense and security.**

Health and Safety

On July 9, 1998, NRC informed Treasury that a pre-decisional memorandum discussing USEC was inappropriately released in NRC's public document room. We understand that the memorandum included a recommendation that USEC receive a "poor performance" rating for the Portsmouth, Ohio gaseous diffusion plant. NRC's Office of General Counsel stated that the pre-decisional memorandum was subsequently removed from the public document room, and NRC has asked that Treasury not consider this memorandum as an official or final position.[15] On July 16, 1998, NRC, in a separate matter, announced a proposed fine against USEC due to alleged inadequacies in USEC's maintenance and testing program for safety-related valves at the Portsmouth, Ohio plant.

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[14] These companies are USEC Inc., the holding company whose stock is being sold to the public; United States Enrichment Corporation; and USEC Services Corporation.

[15] Exhibit E. Letter, dated July 9, 1998, from Malcolm R. Knapp, Acting Director of the Office of Nuclear Material Safety and Safeguards.

Prior to the establishment of USEC as a government corporation, the operation of the gaseous diffusion plants by DOE was not subject to NRC regulatory oversight. As described in the June Memorandum, USEC has taken measures to upgrade the plants to meet NRC regulatory concerns and must continue to address NRC concerns after privatization. We understand that the proposed fine described above is consistent with actions taken by NRC against USEC in the past, as described in the Registration Statement. The possible rating of "poor performance" appears to be substantively different from prior NRC actions. Because the memorandum is pre-decisional and does not represent an official decision by NRC, however, Skadden Arps and USEC management have determined that there is no obligation to disclose the information in the Registration Statement. While the continuing issues with the operation of the Portsmouth, Ohio plant are problematic, we have no reason to expect that privatization will result in reduced attention to regulatory compliance matters, and we have no reason to question the ability of NRC to adequately regulate USEC after privatization. NRC has not recommended that we delay the privatization based on these factors.

Common Defense and Security

Subsequent to our June 28, 1998, decision to proceed with the Offering, the Administration has received a number of expressions of concern regarding national security aspects of the privatization. Some have expressed concerns about the possible effect of USEC's projected uranium sales on the agreement now being negotiated between Russia and western companies to sell Russia's natural uranium. Some have also questioned whether USEC's commercial interests may be in conflict with its role as Executive Agent under the Russian HEU Agreement.[16] These issues have been discussed by the interagency groups since the initiation of the privatization process in 1995. In response to heightened concern with these issues, consultations took place over the last month among senior officials of Treasury, the Office of the Vice President, the National Security Council ("NSC"), the Council of Economic Advisers, the National Economic Council, the Department of State ("DOS"), DOE, and OMB.[17] On July 21, 1998, USEC provided DOS with written clarifications of its policies and plans with respect to completed sales of natural uranium, an elaboration of its statements made in the Registration Statement of its intent to sell natural uranium, and its views on the importance of remaining the Executive Agent for the Russian HEU Agreement.[18] On July 20, 1998, senior Administration officials met with Senator Domenici to discuss these issues. We understand that on July 22, 1998, Samuel R. Berger,

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[16] Exhibit 9. Letter dated June 26, 1998, from Senator Pete V. Domenici to Sandy Berger. Letter dated July 16, 1998, from Major General William Burns, Thomas Neff, John P. Holdren, and Graham T. Allison to President Clinton. Letter dated July 20, 1998, from Senator Domenici to Acting Secretary Elizabeth Moler, Leon Fuerth, Larry Stein, Jim Steinberg and Joshua Gotbaum.

[17] The Enrichment Oversight Committee, chaired by the NSC, met on July 2 and 16, 1998. On July 17 and 20, 1998, the NSC Deputies chaired two sessions on the USEC privatization. On July 20, 1998, representatives from the NSC Deputies met with Senator Domenici.

[18] Exhibit 11. Letter dated July 21, 1998, from USEC Chairman William Rainer and President and CEO Timbers to Acting Under Secretary Holum.

Assistant to the President for National Security Affairs, advised President Clinton that, notwithstanding the national security issues raised, the privatization of USEC should proceed. Additionally, DOS has informed us that it concurs with Mr. Berger.

Accordingly, to our knowledge, no event or condition has occurred since June 28, 1998, that would cause us to change our assessment that the Board's conclusion that privatization through the Offering will not be inimical to the health and safety of the public or the common defense and security, is supported by the evidence and in accordance with the requirements of the Atomic Energy Act of 1954, as amended.

(4) **Privatization through the Offering will provide reasonable assurance that adequate enrichment capacity will remain available to meet the demands of the domestic electric utility industry.**

To our knowledge, no event or condition has occurred since June 28, 1998, that would cause us to change our assessment that the Board's conclusion that privatization through the Offering will provide reasonable assurance that adequate enrichment capacity will remain available to meet the demands of the domestic electric utility industry, is supported by the evidence and in accordance with the requirements of the Atomic Energy Act of 1954, as amended.

Requirements of the USEC Privatization Act

Under the USEC Privatization Act, the Board is required to determine, with the Secretary's approval, that privatization will satisfy the following statutory criteria.

(1) **Privatization through the Offering will provide for the long-term viability of the Corporation.**

To our knowledge no event or condition has occurred since June 28, 1998, that would cause us to change our assessment that (i) as compared to the Carlyle Consortium proposal, the Offering will provide superior assurance of the long-term viability of the private corporation and (ii) the Board's conclusion with respect to the long-term viability of the corporation is appropriate and in accordance with the requirements of the USEC Privatization Act.

(2) **Privatization through the Offering will provide for the continued operation of DOE's gaseous diffusion plants.**

The Offering is likely to result in the reduction of 600 jobs, 100 jobs through attrition, at the gaseous diffusion plants operated by USEC in Paducah, Kentucky and Portsmouth, Ohio over the next two fiscal years. USEC has entered into two agreements with the DOE to ameliorate the effect of staff reductions. Under the first agreement, DOE will assume responsibility for a certain amount of depleted uranium generated by the privatized company for a payment of $50 million

from USEC's pre-privatization funds. DOE will apply these funds through its "work for others" program for two purposes. First, DOE will initiate research and development for the establishment of a facility to treat the depleted uranium. If constructed, the new facility would create a significant number of jobs. Second, DOE will establish a canister maintenance program to enhance the protection of the depleted uranium. DOE has stated its intention to give hiring preferences under its canister maintenance program to qualified USEC workers that are affected by the staff reductions. Under the second agreement to ameliorate the effect of job reductions, USEC is providing certain worker transition assistance benefits using $20 million from USEC's pre-privatization funds.

The disposition of depleted uranium is also addressed by legislation unanimously adopted by the Senate on July 16, 1998, and adopted by the House on July 20, 1998. We expect that the legislation will be signed into law prior to the closing date. The legislation will set aside approximately $385 million from USEC's revenue account and will direct DOE to prepare, by fiscal year 2000, a plan for applying these funds to the disposal of depleted uranium and the construction of onsite disposal facilities at each of the gaseous diffusion plants operated by USEC.[19]

On June 27, 1998, USEC entered into a letter agreement with Treasury in which it agreed that, in the event of the Offering, it would contractually commit to operate the gaseous diffusion plants until January 1, 2005, unless a significant event occurs that could threaten USEC's viability or the maintenance of a reliable domestic enrichment industry. By a letter to Treasury dated July 10, 1998, USEC clarified some of the exceptions to its obligation to operate the plants, and provided assurance that current projections do not anticipate the occurrence of events that would allow plant closings under these exceptions.[20] The provisions of the Agreement Regarding Post-Closing Conduct relating to the gaseous diffusion plants were revised to reflect USEC's clarification, and this Agreement was signed on July 14, 1998.[21]

Accordingly, to our knowledge, no event or condition has occurred since June 28, 1998, that would cause us to change our assessment that (i) as compared to the Carlyle Consortium proposal, the Offering will provide superior assurance of the continued operation of the gaseous diffusion plants, and (ii) the Board's conclusion with respect to continued operation of the plants is appropriate and in accordance with the requirements of the USEC Privatization Act.

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[19] Congress' action is suggestive of widespread support for privatization.

[20] Exhibit 12. Letter dated July 10, 1998, from William J. Rainer and William H. Timbers, Jr. to Gary Gensler, and analysis provided by USEC staff.

[21] Exhibit 13. Agreement Regarding Post-Closing Conduct, dated July 14, 1998.

(3) Privatization through the Offering will provide for the protection of the public interest in maintaining a reliable and economical domestic source of uranium mining, enrichment and conversion services and industries.

As noted above, USEC will have approximately 75 million pounds of natural uranium in its inventory. We note, however, that the worldwide annual demand for natural uranium is approximately 160 million pounds and that, as discussed above in connection with the statutory criterion related to national security, USEC has stated its intention to sell its natural uranium gradually into the market.[22]

Accordingly, to our knowledge, no event or condition has occurred since June 28, 1998, that would cause us to change our assessment that (i) as compared to the Carlyle Consortium proposal, the Offering will provide superior assurance of protecting the public interest in maintaining a reliable and economical domestic source of uranium mining, enrichment and conversion services, and (ii) the Board's conclusion with respect to this statutory criterion is appropriate and in accordance with the requirements of the USEC Privatization Act.

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[22] Exhibit 15. Draft Summary of Key Aspects of the Nuclear Fuel Industry, dated July 20, 1998. Prepared with the technical assistance of Philip G. Sewell, USEC Vice President, Corporate Development.

(4) To the extent consistent with the other statutory provisions, privatization through the Offering will provide the maximum proceeds to the United States.

As discussed above, the net privatization proceeds, including the net Debt Proceeds, are approximately $1.873 billion. This amount is approximately the same as the amount of $1.877 billion, estimated by J.P. Morgan as the net proceeds of the Carlyle Consortium proposal (without giving effect to the six-year $100 million escrow that would be established under the proposal).[23] However, as noted in the June Memorandum, there are significant differences in the non-price statutory criteria between the two proposals.

Accordingly, to our knowledge, no event or condition has occurred since June 28, 1998, that would cause us to change our assessment that (i) the Offering will, in a manner consistent with the principles set forth in Section 3103(a) of the USEC Privatization Act, provide the maximum proceeds to the United States, (ii) the Board's conclusions with respect to this criterion are appropriate and in accordance with the requirements of the USEC Privatization Act, and (iii) the Secretary should determine, pursuant to Section 3103(c) of the USEC Privatization Act, that the Offering will provide the maximum proceeds to the Treasury consistent with the principles set forth in Section 3103(a).

[23] As discussed above, USEC's pre-privatization funds are not considered as proceeds of privatization. Accordingly, the $70 million obligated by USEC from these funds in connection with agreements with DOE regarding depleted UF_6 and worker assistance do not affect the calculation of proceeds.

DEPARTMENT OF THE TREASURY
WASHINGTON

ASSISTANT SECRETARY

The Honorable Tom Bliley
Chairman
Committee on Commerce
U.S. House of Representatives
Washington, DC 20515

Dear Mr. Chairman:

In recent discussions with Under Secretary Gary Gensler, House Committee on Commerce (the Committee) staff requested that the Treasury Department provide the Committee with certain information concerning the privatization of the United States Enrichment Corporation (USEC). This letter responds to that request.

Specifically, Committee staff asked Treasury to provide the following information: (1) the fees charged by financial intermediaries for the USEC initial public offering (IPO) compared with the fees that would have been charged if there had been a merger or acquisition (M&A), and (2) Treasury's examination of separative work units (SWU) price volatility and its effects on USEC's viability and ability to serve as the U.S. Government's Executive Agent.

In response to your first request, the enclosed chart provides a comparison between IPO fees and M&A fees. In response to your second request, we conducted a search of our records for relevant information. We were unable to locate any documents containing analyses of SWU price volatility and its effects on USEC, and none of the current Treasury employees we questioned regarding SWU price analysis work recalled participating in any such efforts. We were informed that Peter Necheles (a former policy advisor at the Treasury Department) recalled having several discussions with Department of Energy staff concerning the effects of SWU price scenarios on USEC's willingness to continue to serve as Executive Agent, but we have not found any written accounts of such discussions in our files.

Please do not hesitate to contact me if you have further questions concerning this matter.

Sincerely,

Linda Robertson

Linda L. Robertson
Assistant Secretary
(Legislative Affairs and Public Liaison)

Enclosure

COMPARISON OF FEES FOR USEC PRIVATIZATION[1]

IPO

Entity	Fee[2]
Morgan Stanley (Lead Manager)	4.8 million
Merrill Lynch (Co-Lead Manager)	4.8 million
Syndicate of Underwriters	32.6 million (List Attached)
Total Underwriting Fees	$42.3 million[3]
J.P. Morgan (Financial Advisor)	$11.8 million

M&A

Entity	Fee[4]
Morgan Stanley (Transaction Manager)	$ 7.6 million
J.P. Morgan (Financial Advisor)	$11.5 million

[1] This chart does not contain a comparison of legal fees. The law firms involved charged hourly rates. It is therefore impossible to determine the legal fees for an M&A that did not occur. On its Form S-1 (filed with the Securities and Exchange Commission), USEC reported $2.1 million in legal fees and expenses directly attributable to the IPO. Legal fees for pre-privatization work that was not directly attributable to the IPO, however, are not publicly available.

[2] The underwriting fees are based on a 2.97% discount of the total proceeds received from the public, prorated to reflect each underwriter's proportion of shares purchased. A total of 100 million shares were sold to the public at $14.25 per share. Morgan Stanley may have received fees exceeding $4.8 million ($4.8 million was computed based on the prospectus), but its net fees were effectively reduced by a $2 million "rebate" payment to Treasury. J.P. Morgan's fee for its role as financial advisor was paid from USEC's cash balances, not out of the IPO proceeds. J.P. Morgan's fee includes payments received over a 3-year period and a success fee received at the time the IPO was completed.

[3] Due to rounding, the amounts shown actually add to $42.2 million, but $42.3 million was the actual total amount.

[4] Morgan Stanley's M&A fee would have been computed by multiplying 0.4% by $1.9 billion, which was the Carlyle Consortium's bid price. J.P. Morgan's fee for its role as financial advisor would have been paid from USEC's cash balances, not out of the proceeds from the M&A.

PROSPECTUS

100,000,000 Shares

USEC Inc.

COMMON STOCK

Of the 100,000,000 shares of common stock (the "Shares") offered hereby, 90,000,000 Shares are being offered initially in the United States by the U.S. Underwriters and 10,000,000 Shares are being offered initially outside the United States and to foreign persons by the International Underwriters. See "Underwriters." All of the 100,000,000 Shares of USEC Inc. (the "Company" or "USEC") offered hereby are being offered and sold by the United States Government (the "U.S. Government"), which is selling its entire interest in the Company. See "Selling Stockholder." The Company will not receive any of the proceeds from the sale of the Shares by the U.S. Government; however, the Company will receive the proceeds, if any, received as a result of the exercise of an over-allotment option granted by the Company to the U.S. Underwriters. Any proceeds received by the Company as a result of the exercise of the over-allotment option will be used to reduce indebtedness of the Company and for general corporate purposes. Prior to this offering, there has been no public market for the common stock of the Company (the "Common Stock"). See "Underwriters" for a discussion of the factors considered in determining the initial public offering price.

The Shares have been approved for listing on the New York Stock Exchange under the symbol "USU," subject to official notice of issuance.

The Company's Certificate of Incorporation sets forth significant restrictions on foreign ownership of shares. See "Description of Capital Stock — Foreign Ownership Restrictions."

SEE "RISK FACTORS" BEGINNING ON PAGE 12 FOR INFORMATION THAT SHOULD BE CONSIDERED BY PROSPECTIVE INVESTORS.

THESE SECURITIES HAVE NOT BEEN APPROVED OR DISAPPROVED BY THE SECURITIES AND EXCHANGE COMMISSION OR ANY STATE SECURITIES COMMISSION NOR HAS THE SECURITIES AND EXCHANGE COMMISSION OR ANY STATE SECURITIES COMMISSION PASSED UPON THE ACCURACY OR ADEQUACY OF THIS PROSPECTUS. ANY REPRESENTATION TO THE CONTRARY IS A CRIMINAL OFFENSE.

PRICE $14¼ A SHARE

	Price to Public	Underwriting Discounts and Commissions (1)	Proceeds to U.S. Government (2)
Per Share	*$14.25000*	*$0.42322*	*$13.82678*
Total (3)	*$1,425,000,000*	*$42,322,000*	*$1,382,678,000*

(1) The Company, after the Privatization (as defined below), has agreed to indemnify the Underwriters against certain liabilities, including liabilities under the Securities Act of 1933, as amended. The U.S. Government will not provide any indemnification to the Underwriters and the U.S. Government will have no liability under the Securities Act of 1933, as amended. See "USEC Formation and Privatization — Certain Restrictions in Connection with the Privatization."

(2) Before deducting expenses estimated at $5.3 million to be paid out of the Company's account at the U.S. Department of the Treasury (the "U.S. Treasury").

(3) The Company has granted the U.S. Underwriters an option, exercisable within 30 days of the date hereof, to purchase up to an aggregate of 10,000,000 additional shares of Common Stock at the price to public, less underwriting discounts and commissions, for the purpose of covering over-allotments, if any. If the over-allotment option is exercised in full, the total price to public, and underwriting discounts and commissions will be $1,567,500,000 and $46,554,200, respectively. The proceeds to U.S. Government will not change by any such exercise, but if the over-allotment option is exercised in full, the Company will receive proceeds in the amount of $138,267,800. See "Underwriters."

MORGAN STANLEY DEAN WITTER
Global Coordinator

MERRILL LYNCH & CO.
Co-Global Coordinator

J.P. MORGAN & CO.
Financial Advisor

The Shares are offered, subject to prior sale, when, as and if accepted by the Underwriters named herein, and subject to the approval of certain legal matters by Davis Polk & Wardwell, counsel for the Underwriters. It is expected that delivery of the Shares will be made on or about July 28, 1998 at the office of Morgan Stanley & Co. Incorporated, New York, N.Y., against payment therefor in immediately available funds.

MORGAN STANLEY DEAN WITTER *MERRILL LYNCH & CO.*

M. R. BEAL & COMPANY
JANNEY MONTGOMERY SCOTT INC.
LEHMAN BROTHERS
PRUDENTIAL SECURITIES INCORPORATED
SALOMON SMITH BARNEY

July 22, 1998

UNDERWRITERS

Under the terms and subject to the conditions in an Underwriting Agreement dated the date hereof (the "Underwriting Agreement"), the U.S. Underwriters named below, for whom Morgan Stanley & Co. Incorporated, Merrill Lynch, Pierce, Fenner & Smith Incorporated, M. R. Beal & Company, Janney Montgomery Scott Inc., Lehman Brothers Inc., Prudential Securities Incorporated and Smith Barney Inc. are acting as U.S. Representatives, and the International Underwriters named below, for whom Morgan Stanley & Co. International Limited, Merrill Lynch International, M. R. Beal & Company, Janney Montgomery Scott Inc., Lehman Brothers International (Europe), Prudential-Bache Securities (U.K.) Inc. and Smith Barney Inc. are acting as International Representatives, have severally agreed to purchase, and the U.S. Government has agreed to sell to them, severally, the respective number of Shares set forth opposite the names of such Underwriters below:

Name	Number of Shares
U.S. Underwriters:	
Morgan Stanley & Co. Incorporated	9,177,893
Merrill Lynch, Pierce, Fenner & Smith Incorporated	9,177,892
M.R. Beal & Company	4,588,843
Janney Montgomery Scott Inc.	4,588,843
Lehman Brothers Inc.	4,588,843
Prudential Securities Incorporated	4,588,843
Smith Barney Inc.	4,588,843
Advest, Inc.	800,000
Robert W. Baird & Co. Incorporated	800,000
Bear, Stearns & Co. Inc.	1,650,000
William Blair & Company, L.L.C.	800,000
Blaylock & Partners, L.P.	1,650,000
J.C. Bradford & Co.	800,000
BT Alex. Brown Incorporated	1,650,000
Chatsworth Securities LLC	225,000
CIBC Oppenheimer Corp.	1,650,000
Credit Suisse First Boston Corporation	1,650,000
Doft & Co., Inc.	225,000
Doley Securities, Inc.	225,000
Donaldson, Lufkin & Jenrette Securities Corporation	1,650,000
A.G. Edwards & Sons, Inc.	1,650,000
EVEREN Securities, Inc.	800,000
Ferris, Baker Watts, Incorporated	225,000
Fifth Third/The Ohio Company	800,000
First of Michigan Corporation	800,000
Friedman, Billings, Ramsey & Co., Inc.	800,000
Goldman, Sachs & Co.	1,650,000
Guzman & Company	800,000
Hambrecht & Quist LLC	1,650,000
J.J.B. Hilliard, W.L. Lyons, Inc.	225,000
ING Baring Furman Selz LLC	1,650,000
Interstate/Johnson Lane Corporation	800,000
Edward D. Jones & Co., L.P.	800,000
Legg Mason Wood Walker, Incorporated	800,000
McDonald & Company Securities, Inc.	800,000
Morgan Keegan & Company, Inc.	800,000
NationsBanc Montgomery Securities, Inc.	1,650,000
Needham & Company, Inc.	800,000

Name	Number of Shares
Nesbitt Burns Securities Inc.	800,000
Ormes Capital Markets, Inc.	225,000
PaineWebber Incorporated	1,650,000
Parker/Hunter Incorporated	225,000
Pryor, McClendon, Counts & Co., Inc.	800,000
Raymond James & Associates, Inc.	800,000
The Robinson-Humphrey Company, LLC	800,000
Samuel A. Ramirez & Co. Inc.	225,000
Schroder & Co. Inc.	1,650,000
Scott & Stringfellow, Inc.	800,000
SG Cowen Securities Corporation	1,650,000
Muriel Siebert & Co., Inc.	1,650,000
Stephens Inc.	800,000
Sturdivant & Co. Inc.	225,000
Sutro & Co. Incorporated	800,000
Utendahl Capital Partners, L.P.	1,650,000
Wasserstein Perella Securities, Inc.	1,650,000
Wheat First Securities, Inc.	800,000
The Williams Capital Group, L.P.	225,000
Subtotal	90,000,000
International Underwriters:	
Morgan Stanley & Co. International Limited	2,250,000
Merrill Lynch International	2,250,000
M.R. Beal & Company	1,100,000
Janney Montgomery Scott Inc.	1,100,000
Lehman Brothers International (Europe)	1,100,000
Prudential-Bache Securities (U.K.) Inc.	1,100,000
Smith Barney Inc.	1,100,000
Subtotal	10,000,000
Total	100,000,000

The U.S. Underwriters and the International Underwriters, and the U.S. Representatives and the International Representatives, are collectively referred to as the "Underwriters" and the "Representatives," respectively. For purposes of the information set forth under this section, the term "Shares" refers to shares of common stock of United States Enrichment Corporation, a Delaware corporation, prior to the consummation of the Holding Company Merger, and shares of common stock of USEC Inc. immediately following consummation of the Holding Company Merger. The Underwriting Agreement provides that the obligations of the several Underwriters to pay for and accept delivery of the Shares offered hereby are subject to the approval of certain legal matters by their counsel and to certain other conditions. The Underwriters are obligated to take and pay for all the Shares offered hereby (other than those covered by the U.S. Underwriters' over-allotment option described below) if any such Shares are taken.

Pursuant to the Agreement Between U.S. and International Underwriters, each U.S. Underwriter has represented and agreed that, with certain exceptions, (a) it is not purchasing any Shares (as defined below) for the account of anyone other than a United States Person (as defined below) and (b) it has not offered or sold, and will not offer or sell, directly or indirectly, any Shares or distribute any prospectus relating to the Shares outside the United States or to anyone other than a United States Person. Pursuant to the Agreement Between U.S. and International Underwriters, each International Underwriter has represented and agreed that, with certain exceptions, (a) it is not purchasing any Shares for the account of any United States Person and (b) it has not offered or sold, and will not offer or sell, directly or indirectly, any Shares or distribute any prospectus relating to the Shares within the United States or to any United States Person. With respect to any

Strategic Plan

September 24, 1997

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KEY ASSUMPTIONS
SWU REVENUE
(continued)

- SWU prices

Year	Estimated New Sales Prices
1998	$ -
1999	95
2000	96
2001	98
2002	100
2003	102
2004	104
2005	106
2006	108
2007	110

  - New SWU prices escalate by approximately 2% per year

- Favorable litigation ruling expected

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1998-SE-007385 (COPY)

Gary FVI
Peter W FVL

The Secretary of Energy
Washington, DC 20585
June 18, 1998

The Honorable Robert Rubin
Secretary of the Treasury
Washington, D.C. 20220

Dear Secretary Rubin:

On July 25, 1997, the President approved a general plan for the privatization of the United States Enrichment Corporation (USEC). In furtherance of that plan, on May 7, 1998, the Treasury General Counsel and the Assistant Secretary for Financial Markets asked the Department of Energy (DOE) and other agencies to provide their opinion on the extent to which several potential transactions would meet certain statutory objectives for the privatization as set forth in the USEC Privatization Act (42 U.S.C. 2297h-1 and 2297h-2).

The Department of the Treasury has asked the Department of Energy's opinion on whether the proposed initial public offering (IPO) provides for the long-term viability of the Corporation, the continued operation of the gaseous diffusion plants, and the protection of the public interest in maintaining a reliable and economical domestic source of uranium mining, enrichment and conversion services (42 U.S.C. 2297h-1(a); 42 U.S.C. 2297h-2(b)).

The Department of Energy has reviewed the material provided by USEC, which includes its strategic plan, a letter from Standard & Poor's with a preliminary credit rating, its draft S-1 registration statement for the Securities and Exchange Commission, its marketing and sales report, and a draft agreement with Treasury regarding USEC's post-closing conduct. Based upon an analysis of these materials and DOE's knowledge of USEC's operations and the nuclear fuel cycle industry, DOE has concluded that the initial public offering (IPO) proposal satisfies the statutory objectives for privatization of USEC. The basis for DOE's determination is provided in the enclosure.

Our two agencies, along with others, have worked long and hard to effect the privatization of the uranium enrichment enterprise since USEC first submitted its plan for privatization to the President in June 1995. We look forward to working with you to bring about its successful conclusion.

Sincerely,

Federico Peña

Enclosure

CONTAINS PROPRIETARY INFORMATION

Enclosure

DOE's conclusion that the proposed initial public offering satisfies the statutory objectives regarding the long-term viability of the Corporation, the continued operation of the gaseous diffusion plants, and the protection of the public interest in maintaining a reliable and economical domestic source of uranium mining, enrichment and conversion services is based upon the following:

The IPO proposal satisfies the statutory objective for long term viability of the corporation, as evidenced by:

- A strategic plan which would, upon implementation, put the corporation into a favorable position to remain a major low cost and reliable provider of uranium enrichment services to the world market, via a plan to continue operating the gaseous diffusion plants (GDPs) until the atomic vapor laser isotope separation (AVLIS) technology is fully deployed.
- A five year track record by management of successfully operating the U.S. enrichment enterprise, including operating the GDPs and serving as Executive Agent for implementation of the U.S./ Russia Highly Enriched Uranium Agreement.
- A demonstrated ability to successfully negotiate and fulfill new and updated contracts to provide enrichment services to both foreign and domestic utilities.
- A financing plan that has obtained a preliminary BBB+ investment grade credit rating from Standard & Poor's.

The IPO proposal satisfies the statutory objective for maintaining a reliable and economical domestic industry, as evidenced by:

- A strategic plan that includes a commitment to deploy the AVLIS technology which, if successful, would enable the corporation to remain a major low cost and reliable provider of enrichment services in the world market.
- A five year track record of aggressively seeking and obtaining enrichment customer contracts extending through 2009.
- A five year track record of improving operations and cost effectiveness of the GDPs.
- A financing plan that has obtained a preliminary BBB+ investment grade credit

rating from Standard & Poor's.

The IPO proposal satisfies the statutory objective for continued operation of the GDPs, as evidenced by:

- A backlog of enrichment contracts with utility customers that can only be satisfied by operation of the GDPs until at least 2003.
- A contractual commitment to keep both GDPs operating through at least January 1, 2005.
- A strategic plan that contemplates operation of the GDPs at least until AVLIS becomes fully operational.
- A strategic plan that includes substantial on-going capital and maintenance expenditures at the GDPs, which would allow the GDPs to remain competitive well into the 21st century. (This assumes new economic power contracts can be negotiated, which the trend toward retail competition should facilitate.)
- A five year track record of operational improvements at the GDPs.

Although DOE's overall position is that the IPO satisfies the statutory objectives for the areas of our special expertise, DOE makes the following general observations:

- The current USEC organization has only been in existence for five years. Although USEC's track record is good, five years is not a long period upon which to base an assessment of long term viability.
- The current Board of Directors will be replaced by a new board following privatization. The new board could replace current management or modify the strategic or financial plans.
- The deployment of the AVLIS technology involves a degree of risk.
- If USEC were unable to renegotiate power contracts as favorable as the current contracts scheduled to expire in 2005 and fail to implement AVLIS in a timely manner, then production costs would increase and consequently challenge the long term viability of the corporation.

July 16, 1998

The President of the United States
The White House
Washington DC 20500

Dear Mr. President:

Circumstances have profoundly changed since you approved the privatization of the U.S. Enrichment Corporation (USEC). Privatization now could seriously undermine one of the most important and successful U.S.-Russian disarmament and nonproliferation initiatives now underway: namely, the purchase of 500 tons of highly enriched uranium (HEU) from dismantled Russian nuclear weapons. We are writing to urge you to put the privatization of USEC on hold until an in-depth national security review can be conducted, taking the new market conditions into account.

Two major changes in circumstances have occurred since privatization was approved, either of which could be enough to imperil the HEU purchase agreement. First, it has been revealed that USEC has tens of millions of pounds more uranium than was previously understood, and plans to sell this uranium at a rate several times the rate envisioned in the USEC privatization legislation. This will make it very difficult for Russia to market the natural uranium component of the blended-down HEU material (particularly in the next few years, when most uranium needs will be met by long-term contracts already in place). Inability to sell this uranium could deprive the hard-strapped Russian economy of nearly a billion dollars in hard currency income over the next five years, giving Russian leaders every reason to break off the agreement (as they have repeatedly threatened to do over problems with the purchase of the natural uranium component in the past). A USEC that remained government-owned, however, could be directed to sell its uranium at a rate that did not interfere with the HEU purchase agreement, as was envisioned in the original privatization legislation.

Second, the price of enrichment services has fallen, to roughly the price at which USEC has contracted to purchase the enrichment component of the blended-down HEU material from Russia. Privatization was approved with the idea that although the U.S. government would no longer have direct control over USEC, it would be able to convince USEC to carry out the government's national security objectives in the HEU deal by holding out the threat that if it did not, the government would designate another firm as executive agent for the deal, and that firm would compete against USEC. Although implementing the HEU deal reduced USEC's profit margins, the argument went, the incentive to avoid competition from another firm acting as executive agent was strong enough to keep the deal moving. But the fall in enrichment prices has completely pulled the teeth from that threat: now, no other firm could make a profit purchasing material from the Russians at roughly the same price for which it could be sold on the market, while competing against USEC's enormous market power (and ability to produce at costs well below the market price). Even if a temporary fix for the uranium component can be found, this fundamental problem with the enrichment component will still pose a serious threat to the future of the HEU purchase. Here, too, the U.S. government's options for addressing the issue are far broader if USEC remains a government-owned corporation than if it becomes a fully private firm.

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We commend you for establishing the Enrichment Oversight Committee in your order of May 26 of this year. We recommend that you direct that privatization be delayed until the Enrichment Oversight Committee can coordinate an in-depth review of the changed impact of privatization on the HEU purchase agreement given these new market circumstances, and make recommendations to you as to whether privatization remains in the U.S. national security interest. The Committee could also review the options available to the government to maintain smooth operation of the HEU purchase agreement if USEC remains a government-owned corporation, or if it is privatized, allowing a side-by-side comparison. Such a delay would also avoid the potential impact on U.S.-Russian relations of the current schedule, under which USEC would reportedly be privatized, thereby undermining prospects for a major source of income to Russia, just before Vice President Gore meets with Russian Prime Minister Kirienko in Moscow.

Under ordinary circumstances, privatization of government operations performing private market functions is highly desirable. In the present situation, however, we believe that a major national security initiative of the U.S. government cannot be left solely in the hands of a privatized firm bound to its shareholders to pursue only their private gain. We urge you to take action in the few days remaining before privatization takes place to ensure that your Administration's national security objectives are fully protected.

Respectfully,

Maj. Gen. William F. Burns (USA, Ret.)

Former Special Envoy, Safe, Secure Dismantlement Talks; Chief negotiator, U.S.-Russian HEU Purchase Agreement

Thomas L. Neff*

Senior Member,
Center for International Studies, MIT
Originator of the proposal for a U.S.-Russian HEU Purchase Agreement

John P. Holdren*

Heinz Professor of Environmental Policy, John F. Kennedy School of Government, Harvard University; U.S. Co-Chairman, U.S.-Russian Independent Scientific Commission On Disposition of Excess Weapons Plutonium

Graham T. Allison*

Director, Belfer Center for Science and International Affairs, John F. Kennedy School of Government, Harvard University; Former Assistant Secretary of Defense for Policy and Plans

*Affiliations for identification only

cc: Al Gore, Vice President of the United States
Kerri-Ann Jones, Acting Director OSTP
Elizabeth A. Moler, Acting Secretary of Energy
William P. Cohen, Secretary of Defense
Sandy Berger, National Security Advisor
Robert E. Rubin, Secretary of the Treasury
Madeleine K. Albright, Secretary of State

JPMorgan

June 15, 1998

J.P. Morgan Securities Inc.

60 Wall Street
New York NY
10260-0060

DRAFT

The Honorable Gary Gensler
Assistant Secretary of Treasury
Department of Treasury
1500 Pennslyvania Ave., N.W.
Washington, D.C. 20220

Dear Secretary Gensler,

You have requested our view of whether United States Enrichment Corporation (the "Company") should implement its proposed privatization through a private sale (a "Sale") to a consortium composed of The Carlyle Group ("Carlyle"), Lockheed Martin Corporation and BWX Technologies, Inc. (the "Consortium") or an initial public offering of equity securities of the Company (an "IPO") as outlined in the Company's Strategic Plan dated September 24, 1997 (the "Strategic Plan").

In arriving at our view, we have reviewed (i) certain internal financial analyses and forecasts concerning the Company outlined in the Strategic Plan; (ii) Carlyle's financial analyses and forecast of the entity that would result from a Sale ("Newco") as outlined in the business plan provided by Carlyle dated May 27, 1998, portions of the financial model of Newco and Carlyle's acquisition proposal, received by us on May 30, 1998; (iii) certain publicly available information concerning certain other companies engaged in businesses that appear to be comparable to those of the Company; (iv) certain agreements with respect to credit obligations of Carlyle; (v) audited financial statements of the members of the Consortium; (vi) the terms of the draft purchase agreement providing for a Sale dated as of May 28, 1998 and the draft registration statement on Form S-1 providing for an IPO dated as of May 26, 1998; and (vii) and other information we deemed relevant for our analysis.

It is our understanding that the Board of Directors of the Company has reviewed all of the foregoing materials. We further understand that on the basis of such review and discussion of the privatization alternatives at several formal meetings, the Board of Directors of the Company has concluded that both a Sale to the Consortium and an IPO as outlined in the Strategic Plan broadly satisfy the statutory criteria for privatization as provided in the Atomic Energy Act of 1954, as amended by the Energy Policy Act of 1992, as well as the Company Privatization Act. In order to assist the Department of Treasury in choosing between the two alternatives, we are offering our view in this letter. A similar letter has been provided to the Board of Directors of the Company.

Based on the IPO valuation range determined by Morgan Stanley Dean Witter ("Morgan Stanley") and Merrill Lynch & Co., and set forth in Morgan Stanley's presentation to the Board of Directors of the Company on June 2, 1998, it is our view that an IPO provides the United States with the opportunity to realize greater proceeds than a Sale to the

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Consortium. In addition, we agree with the view of the Board of Directors of the Company that the Strategic Plan offers the Company an enhanced ability to satisfy the following four statutory criteria: (i) adequate enrichment capacity; (ii) reliable and economical domestic industry; (iii) the continued operation of GDP operations: and (iv) long term viability, albeit with somewhat additional investment risk relative to the Consortium's plan. An IPO, because it incorporates less leverage than the Sale, further provides the Company with increased financial flexibility and lower financial risk to meet these criteria.

On the basis of and subject to the foregoing, it is our view that the Company should implement its proposed privatization through an IPO.

In giving our view, we have relied upon and assumed, without independent verification, the accuracy and completeness of all information that was publicly available or was furnished to us by either the Company or Carlyle or otherwise reviewed by us, and we have not assumed any responsibility or liability therefor. We have not conducted any valuation or appraisal of any assets or liabilities, nor have any such valuations or appraisals been provided to us. In relying on financial analyses and forecasts provided to us, we have assumed that they have been reasonably prepared based on assumptions reflecting the best currently available estimates and judgments by management as to the expected future results of operations and financial condition of the Company to which such analyses or forecasts relate. We have relied as to all legal matters relevant to rendering our view upon the advice of counsel.

Our view is necessarily based on economic, market and other conditions as in effect on, and the information made available to us as of, the date hereof. It should be understood that subsequent developments may affect our view and that we do not have any obligation to update, revise, or reaffirm our view. We are expressing no view herein as to the price at which the Company's stock may trade at any future time if the IPO is undertaken.

Very truly yours,

J.P. MORGAN SECURITIES INC.

By: _____
Name: Jim H. Derryberry
Title: Managing Director

United States Department of Treasury

J.P. Morgan's summary analysis of the privatization of the United States Enrichment Corporation

JPMorgan

This presentation was prepared exclusively for the benefit and internal use of The United States Department of Treasury ("Treasury") in order to indicate, on a preliminary basis, the feasibility of a possible transaction or transactions and does not carry any right of publication or disclosure to any other party. This presentation is incomplete without reference to, and should be viewed solely in conjunction with, the oral briefing provided by J.P. Morgan. Neither this presentation nor any of its contents may be used for any other purpose without the prior written consent of J.P. Morgan.

The information in this presentation is based upon management forecasts and reflects prevailing conditions and our views as of this date, all of which are accordingly subject to change. In preparing this presentation, we have relied upon and assumed, without independent verification, the accuracy and completeness of all information available from public sources or which was provided to us by or on behalf of the United States Enrichment Corporation ("USEC") or the Carlyle-Consortium ("Carlyle") or which was otherwise reviewed by us. In addition, our analyses are not and do not purport to be appraisals of the assets, stock, or business of USEC.

Executive Summary

- J.P. Morgan has reviewed the following materials:
  - management's Strategic Plan;
  - Carlyle's acquisition proposal, Newco Business Plan, and Newco financial model;
  - publicly regulated comparable companies;
  - credit obligations, draft S-1, draft purchase agreement; and
  - other information deemed relevant

- J.P. Morgan recommends that USEC implement its proposed privatization through an IPO.

- The following three issues are central to the determination that the IPO alternative better meets the statutory criteria
  - Timing of development and deployment of AVLIS
  - Continued operation of GDPs
  - Financial structure and control post-privatization

- The pages that follow detail J.P. Morgan's analysis

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Note: In preparing this presentation, J.P. Morgan has relied upon and assumed, without independent verification, the accuracy and completeness of all information available from public sources or which was provided to us or which was otherwise reviewed by us. Information in this presentation reflects prevailing conditions and our views as of this date, all of which are accordingly subject to change

Analysis

- Determination of the commercial viability of AVLIS is important for the financial future of USEC
  - Rapid viability determination regarding AVLIS
  - Industry competitiveness and reduced margins
  - Carlyle debt load restricts investment flexibility
  - Maintenance of strong market share

- Carlyle's GDP plan could create financial stress and lessen operating flexibility
  - Short term in nature
  - Uncertainty regarding reconfiguration of cascade system
  - Reliability of domestic supply is negatively impacted

- Financial flexibility and risk are key components of future viability
  - Carlyle's operating cash flows used to repay debt rather than to reinvest
  - Carlyle's plan limits flexibility to defer debt payments
  - Public company governance provides transparency

Summary views

- Based on information currently available, J.P. Morgan believes that an IPO is the appropriate privatization alternative:
  - AVLIS timing
    - Greater ability to invest in key technology to improve cost structure
  - GDP operation
    - Portfolio of supply alternatives maintained and balanced
  - Financial structure
    - Flexibility to reinvest capital in the business (as necessary)
    - Stability
    - Potential to realize higher proceeds

USEC
A Global Energy Company

[redacted]

July 21, 1998

The Honorable John D. Holum
Acting Under Secretary for Arms,
Control and International Security
Affairs/Director, U.S. Arms
Control and Disarmament Agency
Department of State, Room 7208
2201 C Street, NW
Washington, DC 20520

Dear Mr. Holum:

Thank you for your letter dated July 21, 1998, offering USEC the opportunity to (i) provide a summary of its policies and plans regarding its approach to contemplated sales of natural uranium, (ii) elaborate on certain statements regarding natural uranium sales contained in the Prospectus and (iii) provide USEC's view on the continuing importance of maintaining its designation as Executive Agent to USEC's viability in the private sector. As a supplement to our letter to you dated June 5, 1998, we want to allay any concerns that have been raised in recent weeks that the privatized USEC would act to negatively affect the natural uranium market. We reaffirm our commitment to the HEU Agreement and assure you that USEC will dispose of natural uranium in a gradual and flexible manner so that the Company, as well as all participants in the global uranium marketplace, can benefit from the maintenance of a healthy uranium market.

Rational Market Participant. As a participant in the uranium market, USEC will have every incentive to ensure that its sales of natural uranium do not adversely affect market conditions, particularly prices of natural uranium. Disposing of this material incrementally over the next seven years in a flexible manner is entirely consistent with USEC's commercial interests. As a public company with fiduciary obligations to its shareholders, USEC can ill-afford to unsettle this important market.

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6903 Rockledge Drive, Bethesda, MD 20817-1818
Telephone 301-564-3200 Fax 301-564-3201 http://www.usec.com
Offices in Livermore, CA Paducah, KY Portsmouth, OH Washington, DC

We note that those who have expressed concerns over USEC's proposed uranium sales have referred to an industry consultant's future price projections that are lower than USEC's historic cost of natural uranium. These projections are also substantially below those of other analysts. USEC simply would not sell its natural uranium if its actions would cause price decreases of such magnitude. Furthermore, any sales at those levels would dilute future reported earnings, which would be an outcome unacceptable to USEC or any successful private enterprise.

Market Conditions. USEC fully recognizes the importance of not disrupting the market through ill-conceived or poorly-timed introductions of natural uranium, and will not hesitate to defer planned sales to help ensure a stable market. We intend to appropriately modify any of our tentative plans so as to not significantly affect pricing in the natural uranium market. To this end, the Prospectus, on page 17, cautions investors that there can be no assurance that USEC will be able to sell natural uranium in anticipated quantities. The Prospectus also provides that "[t]he quantity of [natural uranium] that USEC will be able to sell in any given year . . . will be dependent on market conditions (including any sales by the U.S. Government out of its inventory) and prices at the time

Most Sales to Occur After Fiscal 2000. As set forth in the Prospectus, the Company does not anticipate making significant natural uranium sales until after fiscal 2000. This is, in part, because most of the world market requirements for uranium through fiscal 2000 have already been purchased under long-term contract. Any sales by USEC prior to fiscal 2000 will constitute only a small fraction of the world market. Moreover, under the Company's Strategic Plan, USEC's sales between 2001-05 would constitute less than 10% of the world market for natural uranium. In any event, it is our intention not to sell at price levels below those described above.

Gradual Sales. As described in the Prospectus, USEC plans to sell its natural uranium gradually, through 2005, with particular sensitivity to market conditions. To the maximum extent possible, USEC plans to implement such sales under long-term domestic and international contracts. Further, as set forth in the Prospectus, USEC expects to retain the equivalent of approximately 5,000 metric tons of natural uranium to meet ongoing operational requirements. We also note that there are certain statutory and contractual restrictions on the ability of USEC to sell its uranium inventory. Such restrictions affect almost 60% of USEC's uranium inventory. For example, under the USEC Privatization Act, USEC may not deliver more than 10% per year of certain uranium received from the DOE for use in the United States. Additionally, sales of certain recent deliveries of natural uranium from DOE must be spread over at least a four-year period.

Reports to Enrichment Oversight Committee. Pursuant to the Agreement dated as of June 19, 1998 between DOE and USEC relating to the Enrichment Oversight Committee, USEC must provide to the Enrichment Committee, among other information, "average price and quantity of sales and other transfers of natural uranium." Additionally, USEC will notify the Oversight Committee prior to making any significant changes in its policies or plans with respect to sales of natural uranium. To augment the Government's ability to monitor USEC's sales of natural uranium, USEC intends to provide such information to the Oversight Committee on a quarterly basis, rather than the annual basis currently provided for in the Agreement. USEC has and will continue to place a high priority on consultation with, and guidance from, the Oversight Committee on all matters associated with the HEU Agreement -- including the importance of successful arrangements for the sale of Russian uranium.

Importance of the HEU Agreement and Oversight Committee. USEC is fully committed to a stable global nuclear fuel market. We believe that this is in our best economic interest. As clearly described in the Prospectus, USEC's role as the U.S. Executive Agent for implementation of this important contract is a core element of USEC's business. In this regard, the Prospectus notes that the HEU Agreement "provides an important strategic opportunity for USEC to introduce additional uranium enrichment services from Russia to the global market on an orderly basis and in a competitive manner that ensures the reliability and continuity of supply to enrichment customers."

USEC remains fully committed to the HEU Agreement. We have expressed our views that it is in our corporate interest to continue to be the Executive Agent of the United States. We believe that it is in our commercial interests to manage the introduction of the Russian material, as opposed to having it managed by someone else. Stated simply, USEC needs to be the Executive Agent to secure its future. We also believe that the U.S. Government needs a healthy, privatized USEC to act as its Executive Agent to facilitate the most cost-efficient downsizing of the Russian nuclear arsenal possible. Given the reality of world markets, USEC firmly believes it must remain committed to maintaining this important intersection of national security and commerce.

We hope that this letter responds to your request and helps address any concerns that have been raised about USEC's actions with respect to natural uranium. Consistent with its long-term commercial interests, USEC will sell its uranium gradually ~~in a flexible~~ manner that first and foremost supports a healthy, stable market, and with a view towards fulfilling its commitment to the HEU Agreement. We understand that fulfillment of our commitments with respect to the sale of natural uranium is a central element of USEC's performance as Executive Agent. USEC looks forward to working with you closely in the years ahead to insure that the commitments made in this

letter continue to successfully meet the objectives of the privatized company and the Government's national security objectives.

Sincerely,

William J. Rainer
Chairman of the Board

William H. Timbers, Jr.
President and Chief Executive Officer

BUSINESS CONFIDENTIAL

100464

DETERMINATION PURSUANT TO THE UNITED STATES ENRICHMENT CORPORATION PRIVATIZATION ACT FOR THE TRANSFERS OF EXCESS DEPARTMENT OF ENERGY URANIUM

Having considered the requirements of the United States Enrichment Corporation Privatization Act of 1996 (42 U.S.C. §§2297h-2297h-13); the current state of the domestic uranium mining, conversion, and enrichment industries; the Department's analysis regarding the potential impacts of the proposed transfers of surplus uranium to the United States Enrichment Corporation; and other pertinent information, I have determined that the transfers of 3.8 million kilograms of uranium as natural uranium hexafluoride (UF_6) and 0.045 million kilograms of uranium as low enriched UF_6 will not have an adverse material impact on the domestic uranium mining, conversion, or enrichment industry. In order to mitigate potential adverse impacts on industry, the Department will restrict the United States Enrichment Corporation's sales of the transferred uranium to a maximum of 35 percent of the total in any single year, with the total quantity to be sold over a minimum of 4 years.

I, therefore, authorize the transfers of 3.8 million kilograms of uranium as natural UF_6 and 0.045 million kilograms of uranium as low enriched uranium as UF_6 to the United States Enrichment Corporation.

Federico Peña
Secretary of Energy

May 18, 1998
Date

AGREEMENT REGARDING POST-CLOSING CONDUCT

THIS AGREEMENT, dated as of July 14, 1998, is by and between the United States Department of the Treasury ("Treasury") on behalf of the United States Government, the United States Enrichment Corporation ("USEC"), a federally chartered corporation, the outstanding capital stock of which is held by the Secretary of the Treasury, on behalf of the United States Government, United States Enrichment Corporation, a Delaware corporation ("USEC Delaware"), USEC Inc., a Delaware corporation ("USEC Inc."), and USEC Services Corporation, a Delaware corporation ("USEC Services") (USEC Delaware, USEC Inc. and USEC Services collectively, the "USEC Companies" and each a "USEC Company"). References herein to USEC shall be references solely to the corporation itself and not to the United States Government or any other agencies or instrumentalities thereof.

WHEREAS, pursuant to the Atomic Energy Act of 1954, as amended by the Energy Policy Act of 1992 (Pub. L. No. 102-486, 106 Stat. 2776) (the "Energy Policy Act"), and the USEC Privatization Act, as enacted in the Omnibus Consolidated Rescissions and Appropriations Act of 1996 (Pub. L. No. 104-134, 110 Stat. 1321, 1321-335) (the "Privatization Act") (collectively, the "Privatization Legislation"), the Board of Directors of USEC (the "Board") has determined that the transfer of ownership of the assets and obligations of USEC to a private corporation and the transfer of the interest of the United States in USEC to the private sector by means of an initial public offering (the "Offering") will satisfy the conditions precedent to privatization established by the Privatization Legislation, and the Secretary of the Treasury has approved such determination; and

WHEREAS, in connection with the Offering, it is contemplated that (i) USEC will be merged into USEC Delaware, with USEC Delaware as the surviving corporation, pursuant to a merger agreement (the "USEC Merger Agreement"); (ii) each outstanding share of the common stock of USEC will be converted into shares of the common stock of USEC Delaware; (iii) all of the outstanding shares of capital stock of USEC Delaware will be sold to certain underwriters (the "Underwriters") to be named in an underwriting agreement among Treasury, USEC, USEC Inc., USEC Delaware and the Underwriters (the "Underwriting Agreement"), at the time and on the date specified in the Underwriting Agreement (the "Closing"); (iv) USEC Delaware will be merged with a wholly owned subsidiary of USEC Inc. formed solely for the purpose of such merger, with USEC Delaware as the surviving corporation, pursuant to a merger agreement (the "USEC Delaware Merger Agreement"); (v) each outstanding share of the common stock of USEC Delaware will be converted into shares of the common stock of USEC Inc.; and (vi) the shares of common stock of USEC Inc. will be offered to the public by the Underwriters; and

WHEREAS, the USEC Companies desire to enter into a contractually binding commitment to operate until at least January 1, 2005 the two gaseous diffusion plants leased to the USEC Companies by the Department of Energy (each a "Plant" and collectively the "Plants") (subject to the terms and conditions specified in this Agreement) and to undertake any workforce reductions at the Plants during the first two years after the date of this Agreement in the manner described in this Agreement; and

WHEREAS, Treasury, USEC and the USEC Companies desire to set forth certain additional agreements among themselves relating to the Offering;

NOW, THEREFORE, in consideration of the foregoing and the agreements contained herein, and as one of the inducements for the Secretary of the Treasury to approve the decision of the Board to privatize USEC by means of the Offering, the parties hereto hereby agree as follows:

1. Post-Closing Conduct.

(a) USEC and the USEC Companies acknowledge that certain obligations are imposed upon USEC and the USEC Companies under the Privatization Legislation. USEC and the USEC Companies shall abide by and comply with the Privatization Legislation, including without limitation, Section 3111(b) of the Privatization Act.

(b) From and after the Closing until the third anniversary of the Closing, the USEC Companies shall not sell, assign, transfer or otherwise dispose of, in a single transaction or a series of related transactions, all or substantially all of the uranium enrichment assets and properties or uranium enrichment operations of the USEC Companies, other than to USEC Inc. or an entity that is directly or indirectly wholly owned by USEC Inc.

(c) USEC and the USEC Companies acknowledge that the provisions of the Privatization Act provide that the Board, with the approval of the Secretary of the Treasury, shall transfer the interest of the United States in USEC to the private sector in a manner that provides for the continuation of the operation of the Plants. Accordingly, from and after the Closing until at least January 1, 2005, the USEC Companies shall continue Operation of both of the Plants; provided, however, that this paragraph shall not restrict the termination by the USEC Companies of the Operation of a Plant if a Significant Event has occurred with respect to such Plant. For the purpose of this paragraph, (i) "Operation" shall mean the use of the Plants for the provision of enrichment services, at a level reasonably determined appropriate by the USEC Companies, and (ii) a "Significant Event" shall mean: (u) any event beyond the reasonable control of the USEC Companies including, but not limited to, fires, floods, acts of God, transportation delays, acts or failures to act of government authorities or third parties, or inability to secure labor, materials, equipment or utilities that prevents the continued Operation of a Plant by the USEC Companies, (v) that the Operating Margin of USEC Inc. is less than 10% in a twelve consecutive month period, (w) that the long-term corporate credit rating of USEC Inc. is, or is reasonably expected in the next twelve months to be, downgraded below an investment grade rating, (x) the Operating Interest Coverage Ratio of USEC Inc. is less than 2.5x in a twelve consecutive month period, (y) a decrease in annual worldwide demand for Separative Work Units ("SWU") to less than 28 million SWU, or (z) a decrease in the average price for all SWU under USEC's long-term firm contracts to less than $80 per SWU (in 1998 dollars). For purposes of this paragraph, (i) "Operating Margin" shall mean (x) earnings plus interest, taxes and any extraordinary, non-recurring charges divided by (y) total revenue. (ii) "Operating Interest Coverage Ratio" shall mean (x) earnings plus interest and taxes divided by (y) gross interest expense. Nothing

contained in this Agreement shall be construed to modify any obligation that USEC or the USEC Companies may have with respect to the Plants under the Lease Agreement between USEC and the Department of Energy dated as of July 1, 1993, as amended, or under any state or federal law, rule, regulation, order or permit applicable thereto.

(d) USEC's Strategic Plan dated September 1997 and adopted by the Board in January 1998 (the "Strategic Plan") contemplates certain reductions in the workforce at the Plants through USEC Inc.'s fiscal year 2000. To the extent commercially practicable, the USEC Companies shall (i) take steps reasonably calculated in good faith to ensure that workforce reductions at the Plants through USEC Inc.'s fiscal year 2000 are conducted in a manner consistent with the Strategic Plan, do not exceed 500 employees, and are effected in substantially equal parts in each of USEC Inc.'s fiscal years 1999 and 2000, (ii) in each of USEC Inc.'s fiscal years 1999 and 2000, seek to achieve such workforce reductions through a program of voluntary separation before instituting a program of involuntary separation, (iii) with respect to such workforce reductions, provide benefits and take other measures to minimize workforce disruptions that are no less favorable to the workforce than would have been the case prior to the privatization of USEC and that are in accordance with the agreement between USEC and the Department of Energy concerning worker assistance to be entered into prior to the Closing. The foregoing provisions (w) shall not be construed to limit employee terminations for cause or workforce reductions through normal employee attrition, (x) shall be subject to any applicable collective bargaining agreements involving the Plants' workforce, (y) shall not be construed to create any third-party beneficiary rights, (z) shall terminate on the second anniversary of the date of this Agreement.

(e) From the Closing until the third anniversary of the Closing, the USEC Companies shall not grant any option, right or warrant to purchase, acquire, or otherwise receive any direct or indirect interest in, or economic benefit from, any shares of the stock of USEC Inc. or any securities convertible into or exercisable or exchangeable for the stock of USEC Inc., either through any bonus, profit sharing, compensation, severance, stock option, stock appreciation right, stock purchase agreement, retirement, deferred compensation, employment, or other employee benefit agreement, plan, or other arrangement for the benefit or welfare of any director, officer or employee of the USEC Companies or otherwise, unless such grant is made pursuant to an agreement, plan or other arrangement that has been validly approved by the shareholders of USEC Inc. at a meeting held at least 180 days after the Closing.

(f) From the Closing until 180 days after the Closing, the USEC Companies shall not (1) adopt any new, or amend any existing, compensation, employment or consulting agreements or arrangements for the benefit or welfare of any person who is listed as an Executive Officer in USEC Inc.'s Registration Statement on Form S-1, or (2) increase the compensation or fringe benefits of any such person as in effect as of the Closing.

(g) USEC and the USEC Companies shall enter into agreements with each of their respective officers and directors, under which each such officer and director shall agree not

to, and to use his or her best efforts to cause members of his or her respective immediate family not to, purchase shares of the Common Stock of USEC Inc. or otherwise acquire or receive any direct or indirect interest in, or economic benefit from, any shares of the Common Stock of USEC Inc. or any securities convertible into or exercisable or exchangeable for the Common Stock of USEC Inc. during a period from the Closing until 180 days after the Closing. Copies of all such agreements shall be provided to Treasury at least 5 business days prior to the Closing.

(h) From the Closing until the second anniversary of the Closing, the USEC Companies shall not hire, contract with, or provide compensation, employment, or other arrangements for the benefit of (i) persons who are or have been members of the Board of USEC on or prior to the date of this Agreement, or (ii) entities in which such persons have a direct or indirect material interest; provided, however, that this Section 1(h) shall not be construed to limit or alter rights of indemnification or contribution provided by any written agreements in effect on the date of this Agreement. For purposes of this Section 1(h), the parties intend that the term "direct or indirect material interest" shall be construed with reference to Item 404(a) of SEC Regulation S-K (17 C.F.R. § 229.404(a)) and the Instructions thereunder.

(i) For a period of two years after the Closing, the USEC Companies shall not engage, hire, contract with, or provide compensation, employment or other arrangement for the benefit of the financial advisors or law firms that advised the USEC Board of Directors as to the manner and method of transfer of the United States Government's interest in USEC to the private sector without the approval of the Board of Directors of USEC Inc.; provided, however, that this provision shall take effect with respect to each such advisor or law firm only after the expiration of the terms of their respective contracts that are in effect on the date hereof; and provided further, that nothing in this provision shall act to amend, waive or cancel existing contractual limitations on the provision of services to the USEC Companies by such advisors or law firms.

2. Cooperation. The USEC Companies shall provide the Treasury and any other agencies or instrumentalities of the United States Government with such assistance and information, books, records and other material documents of USEC existing on the Closing ("Records"), without charge, as may be reasonably requested by such parties in connection with (i) claims relating to the period prior to the Closing for which the United States Government may have liability, or (ii) the privatization of USEC. Such cooperation shall be provided to the requesting party promptly upon its request and shall include making employees available on a mutually convenient basis to provide additional information and explanation of any material provided hereunder. The USEC Companies shall retain all Records for a period of six (6) years following the Closing.

3. Governing Law; Consent to Jurisdiction. This Agreement, and the rights and obligations of the parties hereunder, shall be governed by, and construed and interpreted in accordance with, federal law and not the law of any state or locality. USEC, the USEC Companies and the Treasury hereby irrevocably and unconditionally consent and submit to and waive any objection to the personal and subject matter jurisdiction of, and venue in, the United

States District Court of the District of Columbia or the United States Court of Federal Claims in any action or preceding arising out or relating to this Agreement. USEC, the USEC Companies and Treasury agree that such jurisdiction and venue shall be exclusive with respect to any such action or proceeding brought by it hereunder. USEC, the USEC Companies and Treasury consent to the service of copies of the summons and complaint and any other such process which may be served in any such action or proceeding by certified mail, return receipt requested, or by any other method permitted by law.

4. Amendment; Waiver. This Agreement may only be amended by an instrument in writing signed by the parties hereto. Any failure by USEC or the USEC Companies to comply with any obligation, covenant or agreement herein may be waived by Treasury, and any failure by Treasury to comply with any obligation, covenant or agreement herein may be waived by USEC or USEC Inc.; provided, however, that any such waiver may be made only by a written instrument signed by the party granting such waiver. Any waiver or failure to insist upon strict compliance with such obligation, covenant, agreement or condition by a party hereto shall not operate as a waiver of, or estoppel with respect to, any subsequent or other failure by any other party hereto.

5. Entire Agreement. This Agreement constitutes the entire agreement between the parties hereto with respect to the specific subject matter hereof and supersedes all other prior agreements and understandings, both written and oral, between the parties with respect to the specific subject matter hereof.

6. Successors and Assigns. This Agreement shall be binding upon and inure to the benefit of the parties and their respective successors and assigns.

7. Notices. All notices, requests, claims, demands and other communications hereunder shall be in writing and shall be given (and shall be deemed to have been duly given upon receipt) by delivery in person, by facsimile or by registered or certified mail (postage prepaid, return receipt requested), to the other party as follows:

If to Treasury:

Department of the Treasury
1500 Pennsylvania Avenue, N.W.
Washington, D.C. 20220
Attention: Assistant Secretary (Financial Markets)

If to USEC or the USEC Companies:

United States Enrichment Corporation
2 Democracy Center
6903 Rockledge Drive
Bethesda, MD 20817
Attention: General Counsel

or to such other address as the person to whom notice is given may have previously furnished to the other in writing in the manner set forth above.

8. Counterparts. This Agreement may be executed in two or more counterparts, each of which shall be deemed to be an original, but all of which shall constitute one and the same agreement.

IN WITNESS WHEREOF, each of the parties has caused this Agreement to be executed on its behalf by its duly authorized representative, all as of the day and year first above written.

THE UNITED STATES OF AMERICA,
acting through the Secretary of the Treasury,
through his duly authorized designate

By: _____

Name: Gary Gensler

Title: Assistant Secretary (Financial Marke

UNITED STATES ENRICHMENT
CORPORATION, a federally chartered corporation

By: _____

Name: William H. Timbers, Jr.

Title: President and CEO

UNITED STATES ENRICHMENT CORPORATION, a Delaware corporation

By: _____

Name: William H. Timbers, Jr.

Title: President and CEO

USEC INC., a Delaware corporation

By: _____

Name: William H. Timbers, Jr.

Title: President and CEO

USEC SERVICES CORPORATION, a Delaware corporation

By: _____

Name: William H. Timbers, Jr.

Title: President and CEO

DEPARTMENT OF THE TREASURY
WASHINGTON, D.C.

ASSISTANT SECRETARY

November 24, 1999

The Honorable Ed Whitfield
U.S. House of Representatives
Washington, D.C. 20515-1701

Dear Mr. Whitfield:

This letter responds to your letter dated September 7, 1999 to Secretary Summers in which you requested that the Treasury Department provide you with certain information regarding the financial condition of USEC Inc.

We are not aware of information that might be construed to indicate that USEC Inc. believes that a "Significant Event" (as that term is defined in the Agreement Regarding Post-Closing Conduct) has occurred. In fact, USEC Inc. has stated on Form 10-Q filed on November 5, 1999, that "[n]one of the exceptions to USEC's obligation to operate the plants has occurred." In the event that USEC Inc. were, at some future date, to conclude that a Significant Event had occurred, the Treasury Department would expect USEC Inc. to explain the basis for its conclusion, and we would independently evaluate the merits of that conclusion, including deciding at that time how we believe the test for determining whether a Significant Event had occurred should be applied.

We provide you with the following information in response to the four questions in your letter regarding specific "Significant Events":

Question 1. Applying the methodology set out by USEC in a letter dated July 10, 1998 from William J. Rainer and William H. Timbers to Under Secretary Gary Gensler, and in a memorandum dated July 20, 1998 from Joel Bryan (Assistant Treasurer at USEC Inc.) to Peter Necheles (a former policy advisor at the Treasury Department),[1] and using data derived from recent USEC Inc. public earnings announcements, which we have not independently analyzed, the operating margin of USEC Inc. during the fiscal year ending June 30, 1999, was 13.1%. The margin was 6.4% for the quarter ending September 30, 1998, 13.1% for the quarter ending December 31, 1998, 8.9 % for the quarter ending March 31, 1999, 18.9% for the quarter ending June 30, 1999, and 13.4% for the quarter ending September 30, 1999. In making our calculations, we first added the following items to net income: interest expense; tax expense; and extraordinary, nonrecurring charges. Next, we subtracted the following items from net income: tax benefits and other income. We then divided that derived amount by revenue. The Treasury Department does not have information that would provide a basis for making estimates about USEC Inc.'s future financial performance.

Question 2. Standard & Poor's downgraded USEC Inc.'s corporate credit, senior unsecured debt, and bank loan ratings from BBB+ to BBB on August 30, 1999. Moody's, however, confirmed USEC's senior long-term debt ratings at Baa1 on July 23, 1999. We note that

[1] Copies of this letter and memorandum have previously been provided to the House Committee on Commerce pursuant to its requests for documents concerning USEC privatization.

Standard & Poor's and Moody's generally consider any rating above BB+ and Ba1, respectively, to be an investment grade rating.

Question 3. Applying the methodology set out by USEC in the July 20, 1998 memorandum referenced above, and using data derived from recent USEC public earnings announcements, which we have not independently analyzed, the operating interest coverage ratio of USEC Inc. during the year ending June 30, 1999 was 5.6x. The ratio was 3.3x for the quarter ending September 30, 1998, 6.5x for the quarter ending December 31, 1998, 3.9x for the quarter ending March 31, 1999, 8.2x for the quarter ending June 30, 1999, and 4.0x for the quarter ending September 30, 1999. In making our calculations, we started with net income, added interest expense and tax charges (or subtracted tax benefits), and divided that amount by gross interest expense. The Treasury Department does not have information that would provide a basis for making estimates about USEC Inc.'s future financial performance.

Question 4. The Treasury Department does not have information about the average price of SWU under USEC Inc.'s current contracts, nor does Treasury have information that would provide a basis for making estimates about the future price of SWU. Treasury notes, however, that USEC Inc. has stated on Form 10-Q filed on November 5, 1999, that "[b]ased on information known, USEC does not anticipate that the average SWU price under its long-term contracts is likely to fall below $80 per SWU (in 1998 dollars) in the near future."

While we have not appointed a single official to serve as an authority on the issues affecting the relationship between the gaseous diffusion plants and the Treasury Agreement, you may contact Kerry Lanham of the Office of Government Financing (622-2460) for questions regarding USEC Inc. In addition, you should feel free to contact me or to have your staff contact Frank Toohey of my office (622-0585).

Sincerely,

Linda Robertson

Linda L. Robertson
Assistant Secretary
(Legislative Affairs and Public Liaison)

Effect of U.S./Russian Highly Enriched Uranium Agreement 1998

Report to Congress Under Section 3112(b)(10) of the USEC Privatization Act

Introduction:

The *Agreement Between the Government of the United States and the Government of the Russian Federation Concerning the Disposition of Highly Enriched Uranium Extracted from Nuclear Weapons (U.S./Russian Highly Enriched Uranium Agreement* or *Agreement)* was signed on February 13, 1993. The 20-year agreement (1994-2013) supports U.S. nuclear nonproliferation policies and mutual U.S. and Russian security interests. The United States agreed to purchase from the Russian Federation 500 metric tons of highly enriched uranium converted to low enriched uranium. The highly enriched uranium is blended down to low enriched uranium under the terms of this Agreement. The resulting enrichment services contained in the low enriched uranium will be sold by the United States Enrichment Corporation (USEC, and now USEC Inc.) to fuel commercial nuclear power plants.

A contract implementing the Agreement was signed on January 14, 1994, with USEC's predecessor acting as executive agent on behalf of the United States and Techsnabexport (Tenex) representing the Russian Government. Tenex is majority owned by the Russian Ministry of Atomic Energy. Under the implementing contract, USEC has agreed to purchase the separative work units contained in the low enriched uranium. Under the amended implementation contract, Russia takes title to the natural uranium component of the low enriched uranium delivered to USEC and is responsible for selling it.

Due to the large quantities of uranium entering the United States under this Agreement, Congress in April 1996 imposed restrictions on the domestic sale of the natural uranium component and established monitoring and reporting requirements. Section 3112(b)(10) of the USEC Privatization Act (Privatization Act) (42 U.S.C. 2297h-10(b)(10)) requires the President to:

1. Monitor the performance of the U.S. executive agent (USEC) under the Agreement, and

2. Report to Congress each year on the effect the low enriched uranium delivered under the terms of the Agreement is having on the domestic uranium mining, conversion, and enrichment industries and on the operation of the gaseous diffusion plants (that USEC operates under a lease agreement with the Department of Energy) including a description of actions taken or proposed to be taken by the President to prevent or mitigate any material adverse impact on these industries or any loss of employment at the gaseous diffusion plants as a result of the Agreement.

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[1]The low enriched uranium being purchased by the United States under this Agreement represents the equivalent of almost 400 million pounds of natural uranium and 92 million separative work units, enough to satisfy about nine years of demand for uranium and separative work units in the United States. Because the uranium is in the form of natural uranium hexafluoride, it also represents over 150,000 metric tons of conversion services.

The purpose of this report is to respond to number 2 above by analyzing the effect of the deliveries under the Agreement on the uranium industries, employment at the gaseous diffusion plants, and actions taken or proposed to be taken to prevent or mitigate any material adverse impacts. This report concludes that there have been no material adverse impacts on the domestic uranium mining, conversion services, or enrichment services industry caused by the deliveries under the Agreement.

Implementation of the Agreement:

The table below shows the quantities of highly enriched uranium that was downblended into low enriched uranium, and their equivalent natural uranium, conversion services, and separative work units delivered. Total ordered quantities for 1998 were not completed during the calendar year.

Delivery Year	Highly Enriched Uranium (metric tons U)	Low Enriched Uranium (metric tons U)	Natural UF_6 Feed Component (Million lbs. U_3O_8(e))	Natural UF_6 Conversion Component (Million kgU)	Separative Work Units (Million SWU)
1995	6	186	4.8	1.8	1.1
1996	12	371	9.5	3.7	2.2
1997	18	480	13.7	5.3	3.3
Total 1998 Orders	24	723	18.9	7.3	4.4
1998 Actual Deliveries	14.5	450	11.5	4.4	2.7

Under Section 3112(b)(1) and (2) of the Privatization Act, the Department took title to the natural uranium component (14.3 million pounds U_3O_8(e)) from the first 18 metric tons of highly enriched uranium (1995-1996 deliveries). Approximately 4.5 million pounds of that has been sold by the Department back to Russia for use in matched sales contracts.[2] Only a small quantity (4.7 million pounds) of the 25.2 million pounds of natural uranium component from the 1997

[2]"Matched sales" refers to one of the methods through which Russian uranium can enter the U.S. market under the Agreement Suspending the Antidumping Investigation on Uranium from Russia (the Suspension Agreement) as amended. Under this provision, Russian uranium is allowed to enter the U.S. market up to a specified volume if the quantity is equally matched with newly produced, U.S.-origin uranium prior to delivery to the ultimate consumer in the United States. The Department of Commerce and the Russians signed an amendment effective October 3, 1996, that allows the natural uranium component to be sold in the United States, thus making the Suspension Agreement consistent with the Privatization Act.

and 1998 deliveries has been sold. The remaining 20.5 million pounds remains in storage at USEC.

During 1998, sale of the remaining Russian natural uranium component was not completed due to various market-related factors and other concerns that would not allow the Russians to receive full value for the uranium. Because of issues surrounding the natural uranium component, Russia delivered, and therefore USEC purchased, 2.7 million of the planned 4.4 million separative work units in 1998. In March 1999, Russia and a Western consortium of producers (made up of Cameco, Cogema, and Nukem, Inc.) did finalize a commercial agreement for the purchase of the uranium contained in future deliveries post-1998. Also in March 1999, a government-to-government agreement between the United States and Russia was executed in which the U.S. Government agreed to purchase the uranium contained in the 1997 and 1998 deliveries as well as to permit a return of a portion of uranium back to Russia.

Effects on U.S. Nuclear Fuel Industries:

Uranium Mining and Conversion Services

Both the uranium mining and conversion services industries are being addressed in this section as both markets experienced the same basic trends for similar reasons. In 1998, both markets experienced a downward pressure in price and decreased contracting activity compared to 1997. Various uranium producers worldwide delayed or reduced plans for production during 1998 due to the depressed state of the market.

Several factors contributed to the market decline; however, the U.S./Russian Highly Enriched Uranium Agreement deliveries to date have not been a significant factor in the market's decline nor have they caused a material adverse impact. Only 8.3 million pounds U_3O_8(e) (4.5 million pounds in matched sales through the Department's contract with Global Nuclear Services & Supply, Ltd.[3] and less than 4 million pounds of sales from the 1997 and 1998 deliveries under the Agreement) have entered the U.S. market to date. This equates to an average of approximately 4 percent of U.S. demand annually during 1995-1998. The recently depressed market was primarily caused by a lack of demand (most utility requirements have already been met through 1999) and an industry perception of a near-term oversupply situation.

Uranium Enrichment Services

On July 28, 1998, the United States Enrichment Corporation, a Government-owned corporation, became the United States Enrichment Corporation, a subsidiary of USEC Inc., a fully privatized

[3] In December 1996, the Department of Energy entered into an agreement with the Russian Federation, through its agent, Global Nuclear Services and Supply, for the sale of up to 7.8 million pounds U_3O_8(e) of the uranium component from the 1995 and 1996 deliveries under the agreement to be sold back to the Russians for use in matched sales pursuant to the Suspension Agreement.

company through an initial public offering on the New York Stock Exchange. In order to "...operate the gaseous diffusion plants more efficiently and to meet foreign competition" (USEC News Release, August 25, 1998), the newly privatized USEC Inc., initiated a voluntary reduction-in-force program for employees at the Paducah, Kentucky, and Portsmouth, Ohio, gaseous diffusion plants. In November 1998, USEC Inc. completed the first phase, eliminating approximately 125 positions at each plant solely through a voluntary reduction-in-force program. The second phase will involve a similar plan of 250 additional reductions in summer 1999.

USEC Inc. pays a price for separative work units under the Agreement that is much higher than its marginal cost of production and higher than current market prices. However, "The Company believes that it is uniquely positioned to act as U.S. Executive Agent" because "it can best integrate this additional supply of enrichment services into the market in a manner that minimizes market impact" (USEC Prospectus, July 22, 1998). Although the Agreement was a contributing factor to the reduction in employment at the gaseous diffusion plants, other considerations included increased competition from foreign enrichment suppliers and a need to improve efficiency, which is normal when a Government entity moves into the private sector.

Actions Taken to Mitigate Adverse Effects:

Enrichment Oversight Committee

On May 26, 1998, President Clinton issued an Executive order for the establishment of the Enrichment Oversight Committee. The committee provides oversight of the executive agent of the Agreement (currently USEC Inc.) and monitors and coordinates all efforts of the U.S. Government with regard to the Agreement. It also collects and analyzes information related to the maintenance of domestic uranium mining, conversion, and enrichment industries. The committee is also responsible for providing this report to Congress, which monitors the effects that the Agreement has on the uranium industry and employment at the gaseous diffusion plants as required by the USEC Privatization Act. The Department has prepared this report on behalf of the committee. A senior official of the National Security Council chairs the committee. Other members include representatives from the Departments of State, Treasury, Defense, Justice, Commerce, and Energy; the Office of Management and Budget; the National Economic Council; the Council of Economic Advisers; and the Intelligence Community.

Uranium Mining and Conversion Services

The U.S. Government took several actions during 1998 that are expected to counter the depressed state of the uranium mining and conversion services markets. On September 22, 1998, in Vienna, Austria, Secretary of Energy Bill Richardson and the Russian Minister of Atomic Energy Yevgeniy Adamov signed an interim joint report on the status of implementation of the Agreement following the requests of Presidents Clinton and Yeltsin at the September 1-2, 1998, Moscow Summit. The joint report moves to facilitate a long-term agreement between Russia and the consortium of Western companies for the purchase of the natural uranium component. The

interim report states that, if the parties are able to reach a long-term agreement, then the Department will take several actions including making a public commitment to defer its own natural uranium sales for ten years. In March 1999, Russia and a Western consortium of producers (made up of Cameco, Cogema, and Nukem, Inc.) did finalize a commercial agreement for the purchase of the uranium contained in future deliveries post-1998. Also in March 1999, a government-to-government agreement between the United States and Russia was executed in which the U.S. Government agreed to purchase the uranium contained in the 1997 and 1998 deliveries as well as to permit a return of a portion of uranium back to Russia

Also, on October 21, 1998, Congress passed, and President Clinton, signed P.L. 105-277 that provides for the United States to purchase, for up to $325 million, the natural uranium component associated with the 1997 and 1998 deliveries (approximately 28 million pounds of U_3O_8(e)) under the Agreement. The purchase of this uranium by the United States is contingent upon Russia and the Western uranium companies reaching a long-term commercial agreement for the purchase of the uranium component associated with enriched uranium deliveries to USEC Inc. in 1999 and beyond. This purchase of up to 28 million pounds of U_3O_8(e), in conjunction with the Department's voluntary moratorium on sales, could provide an additional improvement in the uranium and conversion services market.

Uranium Enrichment Services

While it is recognized that implementation of the Agreement was only one of several factors that could be related to the USEC Inc. layoffs, the U.S. Government took several measures that may result in the mitigation of some job losses at both the Paducah and Portsmouth gaseous diffusion plants. First, the Department signed a Memorandum of Agreement with USEC on June 30, 1998, establishing a $20 million Worker Assistance Fund to minimize work force disruption and assist work force transition at the gaseous diffusion plants. This agreement also provides that the Department shall, where practicable, extend a hiring preference at Department facilities to separated employees, pursuant to existing authorities. A second Memorandum of Agreement was signed on June 30, 1998, where USEC paid the Department an additional $50 million to take and manage 2,026 cylinders of depleted uranium hexafluoride that will be generated postprivatization that also provides that the Department shall, where practicable, extend a preference in the hiring to separated employees at either plant. Furthermore, prior to privatization, USEC committed in a Memorandum of Agreement with the Department of Treasury to ensure that, to the extent commercially practicable, work force reductions would not exceed 250 employees in USEC's fiscal year 1999 and 250 employees in fiscal year 2000 and to seek to achieve such reductions through voluntary separation programs.

Further, P.L. 105-204 provides that the *"Secretary of Energy shall prepare and the President shall include in the budget request for FY 2000, a plan and proposed legislation to ensure that all amounts accrued on the books of the United States Enrichment Corporation for the disposition of depleted uranium hexafluoride [$373 million] will be used to commence construction of, not later than January 31, 2004, and to operate, an onsite facility at each of the gaseous diffusion plants...to treat and recycle depleted uranium..."* Construction and operation

of these facilities would create employment opportunities at the plants.
These Government actions are expected to mitigate some of the impact of layoffs at the gaseous diffusion plants that have occurred from USEC Inc.'s reduction in force.

Conclusion:

In the Administration's judgment, the Agreement did not have a material adverse impact on the domestic uranium mining and conversion services industries during 1998. Due to the outstanding issues surrounding the natural uranium feed component under the Agreement, only a small portion of the uranium was actually sold into the market. Although the uranium mining and conversion services markets were depressed during 1998, it was attributable to the low demand and perception of an oversupplied market. This oversupply should continue to improve and the market stabilize since the uranium feed component issues have been resolved through completion of the government-to-government and commercial agreements signed in March 1999.

The enrichment services contained in the deliveries from the Agreement have been successfully absorbed into the enrichment market through USEC Inc. These deliveries did not cause a direct material adverse impact to the domestic enrichment industry. However, in 1998, the combination of a highly competitive enrichment market and efficiencies sought by USEC Inc. led to reductions in employment at the gaseous diffusion plants. All of those reductions were voluntary. The U.S. Government has taken several actions that may help mitigate these reductions: establishment of a fund to assist in work force transition, providing for a hiring preference at Department facilities, and obtaining a commitment from USEC Inc. to achieve reductions through voluntary separations and to ensure that reductions do not exceed 250 employees in each of USEC Inc.'s fiscal years 1999 and 2000. Additionally, the passage of P.L. 105-204 and the implementation of plans for initiating the disposition of depleted uranium hexafluoride at the gaseous diffusion plant sites will require additional workers. These Governmental actions are expected to have a positive effect on the employment at the gaseous diffusion plants.

PATTON BOGGS LLP
ATTORNEYS AT LAW

2550 M Street, NW
Washington, DC 20037-1350
202-457-6000

Facsimile 202-457-6315

Date:	November 12, 1999
To:	John D. Podesta
Company:	The White House
Fax Number:	(202) 456-1907
Phone Number:	(202) 456-4514
From:	Thomas Hale Boggs, Jr.
Sender's Direct Line:	202-457-6040
Total Pages Including Cover:	3
Client Number:	008714.106

Comments:

John – As you know, there are two problems involving the Russian HEU contract providing for the dismantling of Soviet nuclear warheads: (1) the absence of market-based pricing for Russian SWU and (2) jobs at the two USEC-DOE domestic plants. The attached memorandum describes a way Greg Simon and I believe those problems can be addressed.

Tom

BALTIMORE
DALLAS
DENVER
GREENSBORO
RALEIGH
SEATTLE
WASHINGTON, D.C.

If you did not receive all of the pages or find that they are illegible, please call 202-457-6040.

November 12, 1999

MEMORANDUM

Action Requested

For the reasons set forth in this memorandum, all of the following items need to be acted upon before Congress adjourns this year:

1. Environmental Cleanup and Worker Transition at Oak Ridge, Portsmouth and Paducah. Approximately $175 million will be collected during fiscal year 2000 from utilities and placed in a trust fund for future remediation of uranium and thorium milling sites and the decontamination and decommissioning of USEC's gaseous diffusion uranium enrichment facilities. This $175 million should be made available to DOE for current use for these purposes. Two-thirds of these funds would enable the USEC workers now at risk to continue to be productively employed by DOE contractors and provide cleanup assistance at the Oak Ridge facility as well. Recent press accounts have emphasized the need for acceleration of clean-up activities and it is better policy to redeploy these workers than to terminate them. (The remaining one-third would be used with respect to thorium facilities.)

2. Assistance to USEC for Above-Market Russian SWU. During the period ending December 31, 2001, at least $65 million should be redirected to provide financial assistance to the U.S. Executive Agent (USEC) to offset part of the cost of the payment of above-market prices for Russian SWU through 2001. The legislation should provide that DOE shall make payments to the Russian Executive Agent in an amount equal to the difference between the amount payable for Russian SWU and the spot market price for SWU at the time of purchase of the Russian SWU, with corresponding reductions in the amount payable by USEC for the Russian SWU. The amounts paid to the Russian Executive Agent could be derived from existing no-year appropriations for Russia (P.L. 105-277) to implement the U.S.-Russian accord for the disposition of excess weapons plutonium.

3. Tails transferred from U.S. Executive Agent to DOE. Congress should direct the transfer of depleted uranium from GDP's from the Executive Agent (USEC) to DOE. (Tails generated between 7/28/98 and 12/31/01 in the approximate amount of 24 million kgu). This provides approximately $70 million in value to the U.S. Executive Agent to offset partially their purchase of above market price SWU from Russian nuclear warheads. We are informed that this transfer does not score for budget purposes.

Background

In 1993, the U.S. and the Russian Federation entered into an agreement providing for the peaceful use of highly enriched uranium (HEU) recovered from dismantled nuclear weapons of the former Soviet Union. Under the agreement, Russia converts the HEU into low enriched uranium (LEU). In 1994, on behalf of the U.S. government, USEC (the designated executive agent for the U.S. under the 1993 contract) signed a 20-year agreement with its Russian counterpart to purchase the uranium enrichment component (SWU) of the Russian LEU for resale to utilities for their use in the production of electricity. In 1996, prices for the acquisition of Russian SWU by the U.S. government were set for the five-year period 1997-2001.

When USEC was privatized in July 1998, the acquisition price for Russian SWU was approximately $8 less than the then prevailing SWU market price. Unanticipated and substantial post-privatization declines in the SWU market price have resulted in the payment by USEC, Inc. (the publicly traded private corp.) of above-market prices for Russian SWU. The post-privatization declines in the SWU market price are expected to continue, but Russia has declined to renegotiate the contract to reflect market prices until at least 2002.

There are two problems that must be addressed now in order to protect domestic workers and to ensure that the national security objectives of the United States will continue to be met.

First, as the direct result of the unanticipated declines in the market price of SWU since USEC was privatized in July 1998, USEC has been forced by its legal obligations to its shareholders to consider whether to exercise its contractual right to terminate its status as Executive Agent. Such a termination could raise national security issues and be inconsistent with the nuclear nonproliferation policies of the United States. It is neither USEC's nor the Administration's wish to have that occur.

Second, as part of USEC's cost reduction program, the company will be laying off several hundred DOE and USEC funded workers at its plants in Paducah, Kentucky and Portsmouth, Ohio. If these workers become unemployed, DOE could have substantial liabilities (approximately $30 million) to make payments of "3161 funds" to the affected workers. USEC would prefer that these workers be transitioned to cleanup activities if appropriate funding can be made available.

These two problems can be effectively addressed if all of the three items set forth above are acted upon before Congress adjourns this year.

The Secretary of Energy
Washington, DC 20585

October 28, 1999

Mr. William H. Timbers, Jr.
United States Enrichment Corporation
Two Democracy Center
6903 Rockledge Drive
Bethesda, Maryland 20817-1818

Dear Mr. Timbers:

I have several important issues to bring to your attention.

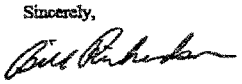
First, as you know, USEC has appealed to the U.S. government for assistance to address costs associated with implementation of the U.S.-Russia HEU Agreement. Indeed, some of these proposals have direct implications for my Department's budget and liabilities. The data USEC has provided to my staff are insufficient to justify your request for assistance of approximately $100 million per year. In particular, the cost data provided are very general and key assumptions are questionable. For example, in the cases examining what USEC could have produced without the HEU Agreement, the electricity and other costs are posited not to rise, potentially exaggerating the cost to USEC of implementing the agreement with Russia. In fact, some of your production may well exceed the cost of buying Russian material. In short, we believe the true financial need may be much lower, or zero. Without better data and documentation of your assumptions, we cannot accurately determine the actual economic impact of the HEU Agreement on USEC. Accordingly, it is difficult to establish the case for near-term government action against that for other corporate actions.

Second, I am concerned about the impact of USEC natural uranium sales on the HEU Agreement. It appears that your market actions may be impacting the foundations of the overall HEU Agreement at the same time you seek our assistance. As you are aware, in March of this year I signed, with Minister of Atomic Energy Adamov, an agreement to address problems on the feed component of the HEU Agreement. The March agreement requires DOE to hold 22,000 metric tons of natural uranium off the market for 10 years, half of which resulted from our purchase for $325 million of a backlog of Russian material. But the market price has declined since that time. Meanwhile, your company's recent earnings statement reports a 100 fold increase in natural uranium sales for the last quarter compared to the same quarter last year, from $200,000 to over $25 million. Such sales may be inconsistent with your written assurances provided to the U.S. last year about responsible marketing of USEC natural uranium inventory. At this rate, you will soon be supplying nearly 25 percent of the U.S. market. What are your plans for natural uranium sales and why should they be viewed as consistent with your previous commitments and the stability of the HEU Agreement? More specifically, what are your current commitments for future deliveries of natural uranium, alone or contained in enriched uranium product, by quarter, for delivery to utilities and other customers?

Third, I am deeply concerned by information that I have learned this month from Minster Adamov regarding how far behind in the delivery schedule USEC has fallen since July. As I understand it, over 400 cylinders were required to complete scheduled deliveries in the second half of this year. As a result of delays by USEC in providing cylinders, Russia will be able to deliver fewer than 300 cylinders to USEC by year's end. Russia will thus lack the means to deliver LEU derived from more than five metric tons of HEU, that will result in more than a $100 million shortfall to Russia. I am also concerned that there is not an agreed schedule for year 2000 deliveries as required by USEC's contract. The timing of these problems is very unfortunate. It undercuts our efforts to urge Russia to move towards market pricing for its enrichment services when the U.S. is seen as not fulfilling basic schedules in the near term. The lack of USEC cylinders to deliver HEU already blended down, and lack of a schedule to blend down more in Russia makes me uneasy about the stability of the path we are on in implementing this critical national security agreement. It also clouds your request for assistance as executive agent. I need credible explanations of these matters.

In closing, I need more and better information to understand how USEC and the DOE should appropriately work together on issues of common concern, such as the HEU Agreement, the future of American enrichment capability and plans affecting the workforce at our GDP sites. In particular, I will be seeing Minister Adamov in the very near future. I would appreciate having written responses on the issues noted above by close of business Friday, October 29 in order to engage Minister Adamov constructively. In addition, my staff will be following up with questions under the appropriate memoranda of information sharing or executive agency.

Sincerely,



Bill Richardson

UNITED STATES
NUCLEAR REGULATORY COMMISSION
WASHINGTON, D.C. 20555-0001

March 29, 2000

Mr. Steven A. Toelle
United States Enrichment Corporation
2 Democracy Center
6903 Rockledge Drive
Bethesda, MD 20817-1818

SUBJECT: USEC FINANCIAL EVALUATION

Dear Mr. Toelle:

Your letter of March 17, 2000, informing us of your delay to provide the financial information we requested on February 25, 2000, is acknowledged. We regret that this information cannot be provided by the date we requested. Because of the importance of this review, we urge you to place a very high priority on providing the requested information.

In your letter you indicated that you will provide financial information through December 31, 2003, the date the current certificates expire. Please be advised that our objective is to perform a financial review considering the next five years, not just through Calendar Year 2003. In the absence of information provided by the United States Enrichment Corporation for the time period requested, our review will be made more difficult.

We agree that a closed meeting to discuss the financial information you are providing would be useful. However, we consider that the meeting should be held as soon as possible after you make your submittal. Please contact Mr. Timothy C. Johnson at (301) 415-7299 to schedule the meeting.

Sincerely,

Melanie A. Galloway

Melanie A. Galloway, Section Chief
Enrichment Section
Special Projects Branch
Division of Fuel Cycle Safety
and Safeguards
Office of Nuclear Material Safety
and Safeguards

Dockets: 70-7001, 70-7002
Certificates: GDP-1, GDP-2

cc: Mr. Randall M. DeVault, DOE-Oak Ridge
Mr. Gary Samore, NSC

March 17, 2000
GDP 00-0045

Ms. Melanie Galloway
Section Chief, Enrichment Section, Special Projects Branch
Division of Fuel Cycle Safety and Safeguards, NMSS
U.S. Nuclear Regulatory Commission
Washington, D.C. 20555-0001

Paducah Gaseous Diffusion Plant (PGDP)
Portsmouth Gaseous Diffusion Plant (PORTS)
Docket Nos. 70-7001 and 70-7002
Response to NRC Request for Information to Support Financial Evaluation

Dear Ms. Galloway:

In Reference 1, the NRC requested the U. S. Enrichment Corporation (USEC) to provide information to support a financial evaluation to be conducted by the NRC. The NRC also requested that this information be provided within 30 days of the date of the NRC letter (viz., by March 27, 2000). The purpose of this letter is to inform the NRC that USEC will provide financial information to support the NRC review by April 14, 2000. This additional time is needed based on the availability of resources in our Finance and Planning group.

In addition, the NRC requested financial information for the next five years. Currently, the NRC certificates for PGDP and PORTS expire on December 31, 2003. As previously discussed with the NRC, USEC has available and will provide financial information to support operation for the remaining term of the certificate and to assist the NRC in making a determination that operation of the GDPs by USEC is "not be inimical to the maintenance of a reliable and economical source of domestic enrichment services." USEC notes that in accordance with draft NUREG-1671, "Standard Review Plan for the Recertification of the Gaseous Diffusion Plants," financial information will be submitted as part of the recertification application to support operation beyond December 31, 2003.

Finally, we consider that it may be beneficial to meet with the NRC to explain the financial information to be provided. To allow the NRC time to become familiar with the information prior to the meeting, scheduling the meeting in late April 2000 appears appropriate. Due to the subject matter, a closed meeting is requested.

If you have any questions regarding this matter, please contact Mr. Mario Robles at (301) 564-3408.

Sincerely,

S. A. Toelle

Steven A. Toelle
Nuclear Regulatory Assurance and Policy Manager

Reference: 1. Letter from Melanie Galloway (NRC) to James N. Adkins (USEC), "USEC Financial Evaluation," February 25, 2000.

cc: P. Hiland - NRC Region III

UNITED STATES
NUCLEAR REGULATORY COMMISSION
WASHINGTON, D.C. 20555-0001

February 25, 2000

Mr. James N. Adkins
Vice President, Production
U. S. Enrichment Corporation
2 Democracy Center
6903 Rockledge Drive
Bethesda, MD 20817

SUBJECT: USEC FINANCIAL EVALUATION

Dear Mr. Adkins:

I am requesting the U.S. Enrichment Corporation (USEC) to provide information to support the U.S. Nuclear Regulatory Commission (NRC) financial review as a result of recent public announcements. On February 3, 2000, USEC announced that it would layoff 850 employees, would cut its annualized dividend from $1.10 per share to $0.55 per share, and would expand its stock repurchase plan to purchase an additional 20 million shares, for a total of 30 million shares, by June 2001. In the announcement, USEC also indicated it is projecting substantially lower earnings for fiscal year 2001 (July 1, 2000 - June 30, 2001). USEC projected fiscal year 2001 net income would be between $35 million to $45 million. Net income for the first six months of fiscal year 2000 was $48.7 million. On February 4, 2000, Standard & Poor's lowered USEC's credit rating from BBB to BB+.

The NRC re-certified USEC's operation of the Gaseous Diffusion Plants in 1999 based, in part, on the finding that USEC would have the financial resources to operate the privatized company and that this operation would not be inimical to the maintenance of a reliable and economical source of domestic enrichment services. This finding recognized that USEC's credit rating at the time was investment grade. Because USEC's credit rating is now below an investment-grade, NRC is again evaluating whether continued operation of the privatized company is not inimical to the maintenance of a reliable and economical source of domestic enrichment services. We will perform the evaluation consistent with the guidance in Chapter 16 of draft NUREG-1671, "Standard Review Plan for the Recertification of the Gaseous Diffusion Plants." To complete this review, we request that you provide the following information identified in Chapter 16:

1. Updated information, not otherwise provided in your current 10-Q and 10-K reports, of the types, amounts, and holders of debt and the types and amounts of equity of USEC. If you have plans for obtaining additional financing, please provide information related to these actions.

2. A five-year business plan addressing the enrichment business line as well as other anticipated business lines, including alternative enrichment technologies such as gas centrifuge and SILEX, that will require investments of capital (including working capital), and the portion of projected revenue, for each of the five years, covered by contracts currently in existence.

3. All significant business and economic assumptions underlying the above plan.

4. Pro forma financial statements for each of the next five years.

5. Any current financial statements, with an independent certified public accountant's opinion of the financial statements, if they differ from the current 10-Q and 10-K reports.

6. Identification of any USEC directors and officers, and a discussion of their qualifications to provide financial and business management, if this information differs from information in current 10-Q and 10-K reports or certification submittals.

7. Any changes in the USEC organizational structure and its relationship to corporate parents and other affiliates, in this information differs from information in current 10-Q and 10-K reports or certification submittals.

8. Information on the financial condition of USEC parent corporations, including credit ratings, profiles prepared by the investment industry, or audited financial statements reflecting the three most recently completed fiscal years.

Please provide a response to these questions within 30 days of the date of this letter.

If you have any questions regarding these actions, please contact Timothy C. Johnson at (301) 415-7299.

Sincerely,

for

Melanie Galloway, Section Chief
Enrichment Section
Special Projects Branch
Division of Fuel Cycle Safety
and Safeguards, NMSS

Docket 70-7001, 70-7002
Certificates GDP-1, GDP-2

cc: Mr. Steven A. Toelle, USEC-Headquarters
Mr. Randall M. DeVault, DOE-Oak Ridge
Mr. Gary Samore, NSC

ATTACHMENT A

Delivery of Russian LEU
1995-2000
(Equivalent Metric Tons HEU)

Calendar Year	Original Schedule (1/94)		Revised Schedule (11/96)		Actual (As of 2/24/00)	
	Annual	Cumulative	Annual	Cumulative	Annual	Cumulative
1995	10	10	6	6	6.1	6.1
1996	10	20	12	18	12.0	18.1
1997 Delivered in 1997*	10	30	18	36	13.4	31.5
1997 Delivered in 1998*					4.5	36.0
1998 Delivered in 1998**	10	40	24	60	14.5	50.5
1998 Delivered in 1999**					9.5	60.0
1999 Delivered in 1999***	10	50	30	90	14.7	74.7
1999 Delivered in 2000***					6.6	81.3

* TENEX unilaterally halted deliveries to USEC in 1997. Balance of 1997 material was delivered in 1998.

** TENEX unilaterally halted deliveries to USEC in 1998. Balance of 1998 material was delivered in 1999.

*** Deliveries completed in February 2000.

Note: The original and revised schedules call for USEC to purchase 30 metric tons of HEU in CY 2000. USEC has placed an order for 30 metric tons for CY 2000 with deliveries scheduled for the March through November timeframe.

UNITED STATES DEPARTMENT OF COMMERCE
International Trade Administration
Washington, D.C. 20230

June 2, 1998

[redacted]

Peter Necheles
Senior Advisor
Government Financial Policy
U.S. Department of the Treasury
1500 Pennsylvania Ave., N.W. - Rm. 2415 MT
Washington, D.C. 20020

Dear Mr. Necheles:

On July 27, 1997, the President approved a general plan for the privatization of the United States Enrichment Corporation (USEC). In furtherance of that plan, on May 7, 1998, the Treasury General Counsel and the Assistant Secretary for Financial Markets asked the Department of Commerce (Commerce) and other agencies to provide their opinion on the extent to which several potential transactions would meet certain statutory objectives for the privatization as set forth in the USEC Privatization Act (42 U.S.C. 2297h-1 and 2297h-2).

Specifically, 42 U.S.C. 2297h-1(a)(1996) provides that USEC, "with the approval of the Secretary of the Treasury, shall transfer the interest of the United States in [USEC] to the private sector in a manner that provides for the . . . protection of the public interest in maintaining a reliable and economical domestic source of uranium mining, enrichment and conversion services. . . . Similarly, 42 U.S.C. 2297h-2(b)(1996) provides that USEC, "with the approval of the Secretary of the Treasury, shall select the method of transfer and establish terms and conditions for the transfer that will provide . . . for . . . the public interest in maintaining reliable and economical domestic uranium mining and enrichment industries. . . ." Treasury has requested Commerce's opinion on these issues in the particular context of privatization through an initial public offering ("IPO").

As you know, Commerce has a limited role in the USEC privatization process, mainly where that process touches on Commerce's administration of the antidumping suspension agreement between Commerce and the Russian Ministry of Atomic Energy. Pursuant to that agreement, Commerce administers quantitative restrictions covering imports of Russian natural uranium and enrichment; via three other bilateral agreements, Commerce administers quantitative restrictions on imports of natural uranium from Kazakhstan, Kyrgyzstan, and Uzbekistan.

Section 734(l) of Tariff Act of 1930, as amended, requires that each uranium suspension agreement "prevent the suppression or undercutting of price levels of [domestic natural uranium and enrichment] by imports of" natural uranium and/or enrichment from that country. Thus, Commerce's overriding concern in administering the agreements, and in the privatization process, is the long-term stability of the U.S. market for uranium products. Consistent with that imperative, in conjunction with the U.S. Customs Service, Commerce strictly enforces the quantitative limitations and price restrictions of the suspension agreements under its Tariff Act authority. In addition, pursuant to 42 U.S.C. 2297(h)(b)(9) Commerce administers and enforces the delivery schedule set forth at 42 U.S.C. 2297(h)(b)(5) for the natural uranium associated with imports of low-enriched uranium derived from highly-enriched uranium from the Russian Federation. Earlier this year, Commerce issued detailed procedures providing notice and guidance to all parties regarding its administration and enforcement of that schedule. Through these responsibilities and efforts, Commerce seeks to fulfill its statutory responsibilities by ensuring that all subject uranium products enter the U.S. market in an orderly fashion which minimizes any market disruptions in both the short and long terms.

We have examined carefully the May 1998 report prepared by USEC entitled, "Privatization of USEC Through an Initial Public Offering: Satisfaction of the Statutory Criteria, Analysis of Reliable and Economical Domestic Industry Requirement," ("USEC Report") and believe that it indicates a commitment to the long-term stability of the U.S. market for uranium products, particularly in its stated commitment to managing the sale of its natural uranium inventory "in a manner which will not be disruptive to the domestic uranium market." Further, we note the public announcements contained therein regarding USEC's intention to keep the gas diffusion enrichment plants ("GDPs") at Paducah and Portsmouth open through at least 2004. Finally, we see nothing in the USEC Report indicating that privatization through an IPO would be harmful to maintaining reliable and economical domestic uranium mining, conversion, and enrichment industries and services.

Commerce declines to comment on certain aspects of the USEC Report relevant to USEC's determination and Treasury's approval, including the financial strength of USEC, technical expertise, and track record. Additionally, Commerce emphasizes that any in-depth analysis on its part of whether privatization of USEC through an IPO meets the statutory criteria would require great speculation as to the future of the suspension agreements, as well as future market and political conditions.

Please contact me at (202) 482-2104 if you have any further questions.

Sincerely,

Joseph A. Spetrini
Deputy Assistant Secretary
Group III

ORIGINAL

UNITED STATES ENRICHMENT CORPORATION

- - -

FORTY-FIFTH MEETING

OF THE BOARD OF DIRECTORS

- - -

Fourth Floor Conference Room

6903 Rockledge Drive

Bethesda, Maryland

Tuesday, June 2, 1998

The meeting was convened, pursuant to notice, at 8:32 a.m.

PRESENT:

BOARD MEMBERS:

WILLIAM J. RAINER, Chairman, presiding

WILLIAM BURTON

CHRISTOPHER COBURN

DR. KNEELAND YOUNGBLOOD, JR.

OFFICERS:

WILLIAM H. TIMBERS, JR., President and Chief Executive Officer

GEORGE R. RIFAKES, Executive Vice President for Operations

HENRY Z. SHELTON, Vice President and Chief Financial Officer

ROBERT J. MOORE, General Counsel

sale?

MR. MARKS: Let's say it was a stock for stock deal. I remember one stock for stock utility deal we were involved in, one company had a nuclear facility, the other didn't. It was taking back stock. It turned around and looked for a consultant to give them a view as to the risks in the operations associated with that kind of facility, because it just didn't have that expertise.

But in almost all circumstances we have the buying company is either in the business or knows the business well enough that that's not necessary. As Jim was saying, in a cash deal that's not relevant.

MR. DERRYBERRY: You take the cash and say: Good luck, guys.

MR. HOLZSCHUH: All of the precedent, but for a sensitive privatization, it's not relevant, because there is no viability test.

MR. COBURN: It seems to me we have a problem, because we have a critical technology which we have based our assumptions on for future performance throughout. We have one source of information. Now finally we have several independent, if you count these bidders as being independent, sources seem to disagree with us.

MR. HOLZSCHUH: The only question I'd raise -- and you guys need to address it -- the independence of

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UNITED STATES ENRICHMENT CORPORATION

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FORTY-SIXTH MEETING

OF THE BOARD OF DIRECTORS

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Third Floor Conference Room

6903 Rockledge Drive

Bethesda, Maryland

Wednesday, June 3, 1998

The Board reconvened, pursuant to recess the prior day, at 9:33 a.m.

PRESENT:

BOARD MEMBERS:

WILLIAM J. RAINER, Chairman, presiding

WILLIAM BURTON

CHRISTOPHER COBURN (participating by telephone)

DR. KNEELAND YOUNGBLOOD, JR.

OFFICERS:

WILLIAM H. TIMBERS, JR., President and Chief Executive Officer

GEORGE R. RIFAKES, Executive Vice President for Operations

HENRY Z. SHELTON, Vice President and Chief Financial Officer

ROBERT J. MOORE, General Counsel

P R O C E E D I N G S

CHAIRMAN RAINER: Welcome to the Forty Sixth Meeting of this Board of Directors.

We don't have a tight agenda plan. The idea was to have a night to sleep on the information that we got yesterday and come back and reconvene today and have a general discussion, an opportunity to raise questions, not exactly free form, but not with a highly structured agenda, either.

I will say that we should think in the following terms, and that is, while there's nothing sacrosanct about a quick decision here, we should be looking for ways to get information that will lead us to a decision on the dual path. Although the goal today might be a little ambitious, I would suggest that we have a goal of some kind of interim leaning one way or the other by the end of the meeting today. And if we don't we don't, but let's just set that up as a goal to where we try to get enough information where there's on an interim, not a committed basis, but just this is the way you're leaning or I'm leaning, and just get a sense of that.

The other thing I'd like to do is discuss some of the issues that we have. It is not practical at this moment to bring in an independent knowledgeable, up to date expert on some of the issues that we heard yesterday

that were in conflict with the business plan that management has put together and that this Board has supported now for over four years.

In a way, if you want to describe it -- and this is not original with me -- we had two presentations yesterday, effective presentations in my view, found some sympathetic audience on some topics with some of us. We have not heard comments from someone who ought to know that might be of a different opinion with respect to our own business plan.

Also, we had the advocate for the M&A people yesterday. We have not had anyone -- we have not had anyone speak on behalf of the IPO. And at the risk of knowing that some of us may be tempted to dilute management's argument about the IPO from the standpoint of potential conflict of interest, we know these people pretty well and each of us has his own factor to divide it by. I nonetheless would like to hear management's view, A, of some of the things that were raised yesterday that were opposed to its and our current business plan; and because if management cares to talk about the advantages of an IPO as opposed to an M&A.

This is not rehearsed. I have not asked Nick, his team. If they don't want to, that's fine, too. But if they want to make some comments about the benefits of

way to go.

What is it about AVLIS -- I mean, could they do that and still meet the statutory requirements? Could we sell to such a bidder and still meet the statutory requirements? Is the statute clear on that or can an argument be made that the statute at least implicitly assumes that whoever buys USEC will have a viable AVLIS program going forward?

MR. MOORE: Yesterday J.P. Morgan actually gave a short answer to that question. Tim Ryan spoke up on it. Two things were stated: one, that AVLIS is not in the statutory criteria; however, it is replete through the Congressional history, the discussion of the creation of the company and the privatization, and the anticipation is that AVLIS continues, that that's the anticipation.

That's the read from the statute. So that allows this Board to give AVLIS life. And clearly the cap on AVLIS funding was a cap on government funding, not a cap on funding forever. Which leads one, using the statutory construction approach, the anticipation of the Congress was AVLIS would indeed continue and would continue in a private sector mode or private funding.

If you look at the history of significant government expenditures over the years, clearly the Congress did not intend for this government corporation to

terminate AVLIS and end it on this side of privatization. As a purely legal matter, you have no reference to AVLIS in the criteria, but you have criteria that encompass AVLIS by their broad terms.

The second thing, though, is clearly my reading of the law is that Congress expected AVLIS to continue, but in a private sector mode.

MR. GOLDMAN: Bill, I think the take on that, and it's clear -- in fact, in our discussion yesterday I think Tim was very helpful. If you go back and look at the statute, it's replete with references to AVLIS.

MR. BURTON: Right.

MR. GOLDMAN: And it is clear that the Congress thought that AVLIS was a major asset that they were giving to the company. At the same time, I think it's pretty clear from the statute that as part of creating a private company it was up to that private company as to what to do with it.

So I think that's a circular way of getting back to your question, which is if you believe, based on your experience, that that asset is worthwhile, like the Congress did when they gave it to the company, then you can satisfy viability and reliability and running the facilities with the pursuit of AVLIS. But it fits in: They gave you the resource and you have to make the

decision.

I think that's the way the statute works.

MR. RIFAKES: Can I add a business perspective. In '94 the Board was faced with a decision on what to do for the future. We looked at viability as staying competitive, so we did a study. It took us over a year to do this, and the study looked at three things: continue operating the plants and investing in them; go with AVLIS; or go with centrifuge.

We concluded that the best way to stay in the business was to build AVLIS and to build it as quickly as possible, because the savings -- the sooner you realize the savings, the easier it was to justify the investment. So we ran a series of studies where we did present value analysis of cash flows from the various things, and clearly, based on that analysis, AVLIS was the winner from strictly the business side, staying, maintaining a viable company, a competitive viable company.

I can tell you, a SWU going forward is not going to keep this company competitive and viable. We're seeing a market where the prices are declining. So that's just not the ballgame.

MR. BURTON: Mr. Chairman -- and I appreciate that and I think that's part of what you're talking about they're responding to. That's not the question I'm

asking.

I'm looking right now for some -- what are the bounds of our authority? Does our authority allow us to sell to a bidder who's not going to operate AVLIS? Now, so I'm really looking more at a legal thing, but I think it's something we all have to deal with, because it would be interesting -- I think it's more than informative to know whether that's something we can even consider or not. And if it's not something we can consider, then we need to look at the issue of does AVLIS survive with a business plan that offers the kind of draconian cuts in AVLIS that Carlyle is proposing.

Now, my question to you would be, AVLIS is replete in there, but Congress damn sure knew how to tell the Board what it had to consider when it sold the company, because it listed operation of the GDP's specifically. To me, if Congress intended the Board to require that AVLIS continue operating, it would have been a bullet point in that list, too, right?

MR. GOLDMAN: Right. They left it up to the Board to decide whether or not they could fulfil the criteria with AVLIS.

To answer your question, Bill, where these two things intersect is that, to the extent that the record of this company and this Board is replete with decisions that

say AVLIS is important to remain competitive to the future of this business, then you would be hard-pressed in fulfilling the statutory criteria to reverse positions now in terms of your own record and your interpretation of the statutory criteria, because you have to do that in order to say it's fine to sell to someone who's sort of doing in AVLIS. I think that's the legal interpretation.

MR. MOORE: This Board has followed every stairstep when it comes to AVLIS to the letter. You decided to seek commercialization. You approved funding for that. There's a list in the statute of all the future activities that this Board could take and you have been taking them seriatim.

The reason I believe there is not a continued AVLIS as a ninth criteria is because of the R and D phase that Congress observed in it. GDP's are different; they've been there for 40 years. AVLIS, instead, they have laid out a development plan for this Board to adopt, and indeed step by step you have been adopting it, even to the extent of having language on siting. There's language on AVLIS siting. That gives clear, clear instruction from the Congress that they anticipate that, if the science is sound, that AVLIS will continue its development phase, even to the point of a siting decision, which we would be authorized to do should you choose to do it.

That's in the statute. That to me gives clear explanation of Congress' intent that AVLIS is to continue into the future. Because it's an R and D project, they turned that final decision over to you the Board on whether it continues or not. But they set up all the steps to have it be a viable activity into the future.

MR. BURTON: Now, you have the situation where we had a bidder who came in here yesterday who had some involvement with AVLIS, who says basically you're taking the wrong approach to it; you should take this different approach; and in fact, you can create [illegible] SWU, [illegible] SWU by taking this approach on the GDP's.

My point -- and therefore you can remain competitive like that; that you've been saying you're going to deploy AVLIS in seven years for the last four years and it's still seven years out.

Since Congress gave us the option of doing that, why can't we accept that? You know what I'm saying?

MR. GOLDMAN: I know exactly what you're saying, and I'll go back to the point that I made before, which is you need to reverse your own record with regard to the priorities that you have already determined are the critical issues for the future of this company if you are to now say, even though it was seven before and it's seven now, we're still comfortable with 14, because that's what

these guys are basically saying.

And if up to this point this Board had not been comfortable with 14 and has repeatedly made decisions and authorized expenditures of money that relate to the development of this technology, then in interpreting the statutory criteria you'd have to reverse your own direction to accept something that says 14 years. That's the legal analysis.

MR. BURTON: Well, we could do that, right?

MR. GOLDMAN: You could do that.

MR. BURTON: Okay. All right. I'm trying to figure out the bounds of our authority, that's what I'm trying to do.

MRS. GREENE: And would you say that -- the only thing that I would question is your characterization of it as being a reversal of a decision that the Board has made. I think I would phrase it in terms of we got pretty consistent input from our first opportunity to have external sources give us input, that the AVLIS projections were not realistic. And so we may, rather than characterizing it as a reversal, I think you could just as easily characterize it as some additional input that would make us have a more realistic or a somewhat different view of the deployment, a realistic deployment schedule for AVLIS.

question is, well, why are you spending this kind of money at Livermore. And it has to do with licensing, waste disposal, and all the things that you need to go through if you get independent of a DOE facility today, which would slow the program down even further.

We looked long and hard about taking that fence, owning the buildings and moving the fence and getting rid of Livermore, and the consequences of that were something that just were intolerable. I mean, these things have been studied for a long time. I realize there have been delays. That's the nature of R and D. I mean, you just have to expect that. We weren't building a plant. We're still in the development stage.

I find it hard to believe that there will be an AVLIS facility if you have that type of delay and that type of expenditure. That's my opinion. It has nothing to do with M&A or IPO. I'm strictly addressing AVLIS. If there's a need for AVLIS or something to replace those plants, their plan, unless there are details that they've got that they just have not disclosed to us, doesn't get there.

MR. TIMBERS: Let me make a couple points, if I could step in here. First of all, there have been extensive external analysis of AVLIS. This has not just been a management program, it's not been a Board program.

Since 1994 when we stopped AVLIS to take a look at it, there has been one, two, three, four, five, six external independent analyses about whether this is a good program to pursue in different venues: one the total program; NRC licensing; there was two in '94; there was one in 1995; there was one in 1996; and there were two in 1997 -- external professional analysis, unbiased, not trying to do a sales pitch, as Jim indicated.

So that there is substantive documentation about whether this is the correct approach, to check our theory. Every time you go into an R and D project and you're moving into commercial deployment, you always want to be sure that you're right. If we're spending $160 million a year, I want to be damn sure we're right and we're on the right course and we're going to achieve the results that we want to do.

Now, I mention $160 million because that's a key amount, because what we're doing is we're going as far and as fast as we can to bring this into commercial deployment quickly. And it's not just for the sake of bringing equipment on or doing a new R and D project, but it's to help make the company more competitive. It is our decision and our conclusion back in 1994 that, with the trend in the marketplace -- the one thing that was never addressed yesterday was that we're in a competitive

have that referenced.

MR. RIFAKES: We'll do that.

CHAIRMAN RAINER: Okay, thank you.

Chris, do you have anything else to say? Your expertise is generally in this field. What should we be thinking about this part of it?

MR. COBURN: Nick's kind of been interrupted. I'm interested in what he has to say.

CHAIRMAN RAINER: Okay, okay.

MR. TIMBERS: The first element is the competitiveness analysis. We think it's essential, it's essential in terms of the long-term viability of this corporation, to be in a competitive marketplace as soon as we possibly can.

We decided not to do a pilot plant for a couple of reasons, but the most important thing is the marginal benefit of certainty that you gain by a one-line plant was not worth the cost, the time, or the sacrifice of competitiveness. That's the decision we made back in '94, a clearcut decision.

We made the decision not to do, specifically not to do what Carlyle's proposing. And we think that all the test results that we've had over the last 18 months, that it has proven probably to be the right decision.

You're right, Margaret, when we got this thing

MR. BURTON: When will we get a recommendation from you?

MR. DERRYBERRY: I wish I could answer the question.

MR. BURTON: Right now, right now you are neutral?

MR. DERRYBERRY: Right.

MR. BURTON: And Skadden?

MR. GOLDMAN: I think -- and we could get into this in more detail when you want to. As we tried to outline yesterday, I think that we have some serious concerns, as we said, which you have to take a deep hard look at, at the question of whether or not these statutory criteria can be satisfied in view of the leverage issue on the Carlyle transaction, in view of the reinvestment issue relating to the gigantic gap between AVLIS 14 years out versus 7 years out, and in view of the Lockheed track record in performing in terms of the record that Lockheed has in front of this Board and the idea of turning this business over to them in view of that record.

I think we have concerns about all three of those points in the context of the statutory criteria.

MR. COBURN: Les, I just want to know -- and I'm not trying to advocate one position or another at this time, but I think I made the point to someone yesterday,

if you took out Portsmouth we would all be raving about Lockheed. So something is right in the company, but at the same time obviously we have problems.

MR. BURTON: Can I follow up on Les' point? And I appreciate that. I appreciate your candor there. But also, to make sure we understand, you know, Treasury's kind of done the Board a favor by taking us, by eliminating the possibility that we'll serve on the subsequent board, because we really have only what's in the best interest of the shareholder.

CHAIRMAN RAINER: May I interject something?

MR. BURTON: Yes.

CHAIRMAN RAINER: Treasury didn't do that. We did that to ourselves.

MR. MOORE: I think it's healthy. I think it's healthy. I think it's really helpful to understand people's motivation here, and I think for the most part we know where the financial advisers are and we know kind of where management is.

But we haven't really talked about your situation, Les, and just for a second if we could kind of talk about that. The unions did raise it yesterday. You do have a fairly sizable contract with U.S. Enrichment Corporation, your law firm does.

MR. GOLDMAN: I think in terms of all the

advisers we probably have by far and away the smallest.

MR. BURTON: Okay.

MR. GOLDMAN: I don't think there's anything stupendous about our contract.

MR. COBURN: We have the smallest contracts.

DR. YOUNGBLOOD: Yes, exactly.

MR. GOLDMAN: I'll grant you that.

MR. BURTON: But I mean, you have been -- the advisers have come in for purposes of selling the corporation. You have been from ground one. You helped convert this from a Department of Energy function to a very successful government corporation. You've been a part of the team, quite frankly. Albeit an outside contractor, but you've been an important part of the team.

My question is, now, we've got a bidder that's come in, as we talked about, with a very heavily marked-up document. They had their own attorneys with them, a very credible law firm out of Los Angeles. I have no idea what -- and I think we talked a little bit about the fact that Skadden had done some work for Carlyle, but currently is not representing Carlyle.

Has there been any discussions with the Board about -- I mean, with the company, about, in the event of an IPO, whether Skadden would remain the counsel for the new company? Bob, can you?

MR. MOORE: I'd like to take that.

Absolutely not. This company does not, with contractors, does not make promises with regard to one path or the other.

MR. BURTON: Oh, I'm not asking about promises. I'm talking about discussions.

MR. MOORE: I'm saying promises, discussions. That's not the way that we conduct our business. Congress set up the government corporation to operate successfully until the Board chooses to privatize and so we have contracts that are on the books that are over many, many year periods and depend on the skill of the contractors. As long as they continue operating to the satisfaction of the company, they stay. If they're not operating satisfactory to the company, they go. And we retain that flexibility.

But there are no discussions or promises that someone stays with one path, but goes with another path.

MR. BURTON: But isn't it fair to say, though, that generally you, like the Board, has been satisfied with Skadden's performance today and that it's the expectation of all of us that if we go with an IPO that Skadden would remain counsel, at least initially, for the new corporation, versus at least the appearance yesterday it seems like of a fairly, at least a stronger possibility

that Skadden would not be the chief outside counsel for the M&A company?

I'm not saying that that's all factual. If anybody can dispute it, I want to hear that. But it may be something we want to take into consideration in considering recommendations.

MR. GOLDMAN: Bill, might I address that --

MR. BURTON: Absolutely.

MR. GOLDMAN: -- for a second? The single most important -- number one, the answer is there have been no discussions about future employment.

Number two, the single most important thing to Skadden, as is the case in any deal where we work for different parties on different sides at different times - I think it's true of all the advisers -- is the professionalism and the expertise that we bring to bear and acting ethically and properly and giving our best possible advice at any given moment.

In terms of your question as it relates to a view, I would say that since we've been here, since the inception and we've been outside counsel for the company, it gives us some particularly interesting insights into activities, for example related to the conduct of Lockheed, whether it's aggravations in terms of going to meetings, whether it's getting to the NRC, whether it's

following the rules of the contract, on a whole range of insights as to the capabilities of this company.

And I didn't hear anything negative from Lockheed about us. The union was the one who raised it. It wasn't Lockheed. And we haven't worked for them at all.

But I think we're uniquely situated to have insights with regard to who can fulfil the obligations of the statutory criteria. Frankly, I personally go all the way back to having worked on the legislation and participated in the Smith Barney study which created the statutory criteria to begin with. So there are insights there.

When you ask the question of where are we coming from when we give substantive and political advice, in this town -- and I've been doing that for the last 28 years -- I think we come at it from the professional best shot we can give you in answering that question, without a bias for future employment or past gain.

MR. BURTON: Well, and to be fair, my point on the record was that everybody's satisfied with your performance, or at least my understanding is management is; as a Board member I've been very impressed with Skadden's work on this, every aspect of it. I particularly sung the praises of the S-1 recently. And

nobody I think has questioned that.

I just think it's important to understand. For example, quite frankly, I didn't know you go back to the Smith Barney study, which was Nick's introduction to this process, right? So I'm just saying there could at least be a perception -- and unfortunately we're in Washington, so we've got to deal with that perception -- that our legal advisers have a pretty close connection with management. And I don't think there's any question about management's preferences in these two choices.

MR. GOLDMAN: The answer I gave related to the best shot at the statutory criteria, not who would get the job.

MR. RIFAKES: I'm offended at that as a member of management. I'm 64 years old. I'm not looking for a new career. And my job is to see to it that this corporation continues in a viable manner, and that's my choice.

And when I speak about the operating issues, they're independent of M&A or IPO. I personally don't care. I do care to see this corporation continue. So if there is an implication that there is a leaning one way or another, I have to object to that, Bill.

MR. BURTON: Well, I regret -- I mean, I regret that you do. I raised it previously with management and

I think what the bottom line here really -- and again, it's a wonderful opportunity for the Board -- is an example here where we just think from a competitive standpoint and the progress that's been made on AVLIS over the last couple of years that this is going to be the method by which this company stays viable on a going forward basis and it's the decision by where we decide to reinvest. Where the IPO would reinvest its cash flow is back into the company rather than retiring debt.

CHAIRMAN RAINER: I have one question and this is for anybody in the room that heard something that could help me, who also would be willing to say. And that is, I asked Allen if their major change in the business plan for AVLIS, slowing it down and so forth, were based on data from where the science is and the R&D is, or from his overall general experience dealing with these things in his career.

He answered both, but I didn't hear the data part too well. Did anyone hear the data part very well? Did he say anything that was substantive that he had some of the same information that we've seen with these results and all that and his analysis were such that, bingo, this drives a new decision to lead to the business plan that they have?

DR. YOUNGBLOOD: I didn't hear any data. I

MR. TIMBERS: Well, I'll let George answer it, but I'll tell you, one thing is that every day that privatization is delayed is delay of deployment of AVLIS, and it's been that way for about two years.

MR. COBURN: Now wait a second. I'm sure that that is partly true, but on the other hand we have had significant technology challenges in the last two years.

MR. RIFAKES: But there are a lot of things on the critical path, including NRC, and until we buy a site, which is beginning deployment, we cannot really start the NRC process.

MR. TIMBERS: As you've seen the schedule slip out, it has been a direct result of the delaying of the licensing and the siting process.

MR. RIFAKES: Right.

MR. TIMBERS: It's not been a technological thing, it's been a siting delay. So that there are 90-day plans in this corporation of what you do 90 days after privatization and the number one thing is to begin the siting process for AVLIS so as to stop this delay of this on a going forward basis.

DR. YOUNGBLOOD: Again, and I mention this point --

CHAIRMAN RAINER: Excuse me, Kneeland.

Did anybody hear any data? This seven-year

Second of all, the plan that is put forth by Carlyle comes out with a unit production cost at the end of the five-year period higher than ours.

So that I think that again, I guess I would characterize as to whether we're biased in this process, I'm very biased. I'm biased to our plan. I'm biased to the AVLIS plan that we have and I'm biased to what I think is a good operating plan that we have, that is reflective of realities of how the plants operate -- keep them going with a proper capital investment for the five-year period at about the same level of investment that the Carlyle Group does and result in a lower unit production cost.

George?

MR. RIFAKES: We've looked at the proposal for the GDP's rather carefully. I've had Jim Miller and others going through it. And there are some apparent inconsistencies and I would just like to point out a glaring one.

On the one hand, they say that they're going to improve union relations. Now, you heard the union yesterday. And on the other hand, they say they're going to reduce 1710 people. How they can achieve both those things is a question that I think needs to be asked, because the reduction in personnel is almost the equivalent of shutting down a plant, and we've all been

way.

You've seen our strategic plan. You have seen that chart that shows how we think we're going to do this and we can do this in a profitable manner.

Number three is to bring AVLIS into commercial deployment on time and on budget. One of the four major central concerns of this company is to do exactly that. I think that it is a challenge. Every one of these things is a challenge. This business is a challenge. But we feel confident in the development that's occurred, that has happened in the last 18 months, in the successes of the AVLIS development, that we can do this.

We have found there are ways that constantly we have been challenged in this business over the last five years. From the very beginning, I was told back in April of 1993: Change the transition date because you'll never do it. We did it. Change the date of NRC certification; you'll never do it. We did it. The same challenge here with AVLIS is to bring AVLIS on line on a timely basis and on budget.

The fourth challenge and opportunity is to strategically grow USEC's business. We believe very strongly, we've believed from the day we started here, sitting at this table, that we should broaden our operational base to go into new business opportunities

UNITED STATES ENRICHMENT CORPORATION

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FORTY-SIXTH MEETING

OF THE BOARD OF DIRECTORS

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Executive Center,

Conference Room

Terminal 3, Concourse H and K

O'Hare Airport

Chicago, Illinois

Tuesday, June 9, 1998

The meeting was convened, pursuant to notice, at [illegible] p.m. CDST.

PRESENT:

BOARD MEMBERS:

WILLIAM C. RAINER, Chairman, presiding

C. WILLIAM BURTON

CHRISTOPHER M[illegible] BURN

[illegible] FREELAND J[illegible] YOUNGBLOOD, JR.

ALSO:

ROBERT J[illegible] MUSE, General Counsel

CHAIRMAN RAINER: And we are liable to come back to it as we talk about these others, but, in and of itself, that is the question. It sounds like we are all pretty comfortable that there is reasonable assurance of enough capacity in both of these strategic plans.

I would like to talk about the gaseous diffusion plants tests. It says here we are directed to set out the method and terms for the transfer of the gaseous diffusion plants that will provide for the continued operation of the Department of Energy's gaseous diffusion plants. This is an interesting one, because -- well, you know what, let me hold that one. I am going to move on to reliable and economically domestic. I am sorry; we will come back to the GDP's

We need to think in terms of what that means. But I would like to move on to this "transfer that will provide for the public interest in maintaining reliable and economical domestic uranium mining and enrichment industries." This is where we're presented with two radically different business plans with respect to AVLIS and the GDP's

Who wants to get started on it?

MR. YOUNGBLOOD: I will simply make the statement that I think both of them feel that they satisfy these criteria. They just do it in radically different

ways, one with an investment in AVLIS and the other an investment, a greater investment in the GDP's.

It is my opinion that I would rather see the investment -- having been here since the beginning of this company -- to have the proceeds of these billion-plus dollars go toward the reinvestment in AVLIS and the success of the company as compared to paying down debt. That is my opinion.

But I think that both of them meet the criteria.

MR. BURTON: Could one of the advisers explain the dividend issue that separates the two proposals before us?

MR. DERRYBERRY: The dividend issue?

MR. BURTON: Yes. Isn't it a thought that the privatized company -- I am sorry -- the IPO company would pay a dividend?

MR. DERRYBERRY: Yes, the IPO company is proposing to pay a dividend. The last number I saw was $110 million.

MR. HOLZSCHUH: It is a function of the size of the deal. It is roughly a 7-percent yield on whatever the deal is.

MR. DERRYBERRY: That dividend is paid to the public investors. The M&A deal, that cash flow, plus the AVLIS cash flow, is essentially used to pay interest and

UNITED STATES
NUCLEAR REGULATORY COMMISSION
WASHINGTON, D.C. 20555-0001

June 23, 1998

OFFICIAL USE ONLY

[redacted]

The Honorable Robert E. Rubin
Secretary of the Treasury
Washington, D.C. 20220

Dear Mr Secretary

On June 5, 1998, the U.S. Nuclear Regulatory Commission (NRC) provided the U.S. Department of Treasury with a recommendation on the ability of the privatized U.S. Enrichment Corporation (USEC), resulting from the initial public offering (IPO) proposal, to meet the USEC Privatization Act (P.L. 104-134) restriction regarding the maintenance of a reliable and economical domestic source of uranium enrichment services. NRC had determined that the proposal would meet the restriction based on a Standard and Poor's credit rating of "A-" for the IPO

Since that determination was provided, USEC has revised the financial structure of the IPO proposal, causing the previous "A-" Standard and Poor's credit rating to become inapplicable. Based on the new financial structure, Standard and Poor's has determined a credit rating of "BBB+ " USEC has provided to NRC the Standard and Poor's credit rating of "BBB+" for the revised IPO proposal. This credit rating was reviewed according to the criteria set forth in NRC's Gaseous Diffusion Plant Certification Standard Review Plan (SRP), Chapter 1.4, "Determination of Foreign Ownership, Control, or Domination, Common Defense and Security, and Reliable and Economical Source of Domestic Enrichment Services." As the credit rating meets the criteria stated in the SRP, NRC has determined that the privatized USEC, resulting from the revised IPO proposal, will meet the USEC Privatization Act restriction regarding the maintenance of a reliable and economical domestic source of uranium enrichment services.

Sincerely,

Shirley Ann Jackson

Shirley Ann Jackson

OFFICIAL USE ONLY

As filed with the Securities and Exchange Commission on June 29, 1998.
Registration No. 333-

SECURITIES AND EXCHANGE COMMISSION
Washington, D.C. 20549

FORM S-1

REGISTRATION STATEMENT
UNDER
THE SECURITIES ACT OF 1933

USEC Inc.

(Exact name of registrant as specified in its charter)

Delaware	2819	
(State or Other Jurisdiction of Incorporation or Organization)	(Primary Standard Industrial Classification Code Number)	(IRS Employer Identification Number)

2 Democracy Center
6903 Rockledge Drive
Bethesda, MD 20817
(301) 564-3200
(Address, including Zip Code, and Telephone Number, including Area Code, of Registrant's Principal Executive Offices)

Henry Z Shelton, Jr.
Vice President and Chief Financial Officer
USEC Inc.
2 Democracy Center
6903 Rockledge Drive
Bethesda, MD 20817
(301) 564-3200
(Name, Address, Including Zip Code, and Telephone Number, Including Area Code, of Agent For Service)

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Approximate date of commencement of the proposed sale of the securities to the public: As soon as practicable after this Registration Statement becomes effective.

If any of the securities being registered on this Form are to be offered on a delayed or continuous basis pursuant to Rule 415 under the Securities Act of 1933, as amended, check the following box. ☐

If this Form is filed to register additional securities for an offering pursuant to Rule 462(b) under the Securities Act, check the following box and list the Securities Act registration number of the earlier effective registration statement for the same offering. ☐

If this Form is a post-effective amendment filed pursuant to Rule 462(c) under the Securities Act, check the following box and list the Securities Act registration statement number of the earlier effective registration statement for the same offering. ☐

If this Form is a post-effective amendment filed pursuant to Rule 462(d) under the Securities Act, check the following box and list the Securities Act registration statement number of the earlier effective registration statement for the same offering. ☐

If delivery of the prospectus is expected to be made pursuant to Rule 434, please check the following box. ☐

CALCULATION OF REGISTRATION FEE

Title of each class of securities to be registered	Number of shares to be registered (1)	Proposed maximum offering price per share (2)	Proposed maximum aggregate offering price	Amount of registration fee
Common stock, par value $.10 per share	110,000,000	$16.50	$1,815,000,000	$535,425

(1) Includes 10,000,000 shares which the U.S. Underwriters have the option to purchase to cover over-allotments, if any.

(2) Estimated solely for purposes of calculating the registration fee pursuant to Rule 457(a).

The Registrant hereby amends this Registration Statement on such date or dates as may be necessary to delay its effective date until the Registrant shall file a further amendment which specifically states that this Registration Statement shall thereafter become effective in accordance with Section 8(a) of the Securities Act of 1933, as amended, or until this Registration Statement shall become effective on such date as the Commission, acting pursuant to said Section 8(a), may determine.

RISK FACTORS

In addition to the other information contained in this Prospectus, the following factors should be carefully considered in evaluating an investment in the Shares.

Risks Associated with Enrichment Operations

Use of Chemicals in Enrichment. The Company's operations at the GDPs involve processes that utilize a large number of different chemicals in significant quantities, many of which are toxic. The primary chemical used by the Company is uranium hexafluoride (UF_6), which is solid under normal conditions, but becomes a gas when heated as part of the Company's enrichment processes. If UF_6, the chemical gas form of uranium processed by the Company, is released into the atmosphere, it reacts with water vapor in the air to create hydrofluoric acid, a highly toxic compound, and uranium, a heavy metal. The primary risk posed by such releases is to humans or animals in close proximity to the releases. In particular, the hydrofluoric acid is highly corrosive and can cause injury if inhaled or if it comes into contact with skin for a prolonged period, and the uranium if ingested can cause kidney damage. The Company follows strict procedures and precautions in the handling, storage and transportation of the materials used in its operations, and there have been no significant releases into the environment in the Company's history. Nevertheless, if an accident were to occur, its severity could be significantly affected by the volume of the release and the speed of corrective action taken by GDP personnel, as well as other factors beyond the Company's control, such as weather and wind conditions.

Dependence on Large Production Facilities. The Company's operations are subject to those risks inherent in operating large scale production facilities. Significant or extended unscheduled downtime at either GDP due to: (i) equipment breakdowns; (ii) power interruptions; (iii) regulatory enforcement actions; (iv) hazards inherent in operating a large scale industrial facility such as labor disruptions; or (v) interruptions caused by potential natural or other disasters, including earthquake activity in the vicinity of the Paducah GDP, could materially adversely affect the Company's operations and financial condition. In particular, as process equipment goes offline, it becomes less cost efficient to produce each SWU. See "Business — GDPs/Operations" and "Business — Employees." Further, in the event of an extended reduction in, or suspension of, operations at the Portsmouth GDP, the Company would be unable to fulfill customer orders solely from the Paducah GDP. In the event of a suspension of operations at the Paducah GDP, the Company could fulfill some, but not all, of the customer orders solely from the Portsmouth GDP. The Company's current and planned insurance policies provide coverage against some, but not all, of its operating risks.

Contractual Commitment to Operate the GDPs. The Company has entered into an agreement with the U.S. Treasury (the "Treasury Agreement") pursuant to which the Company has committed to operate both of the GDPs until January 1, 2005, subject only to limited exceptions, including events beyond the Company's control such as fires, floods and other acts of God, maintenance of certain financial ratios, a significant reduction in the worldwide demand for SWU, a significant reduction in the average price for SWU, or a significant decrease in operating margins, among others. See "USEC Formation and Privatization — Certain Continuing Arrangements Involving the U.S. Government After Privatization." The Company has committed to purchase 5.5 million SWU under the Russian HEU Contract in each of the years 1999, 2000 and 2001, expects to purchase 5.5 million SWU in each of the years following 2001, and could begin enrichment operations at an AVLIS facility in 2004. There can be no assurance that the commitment to continue operations at both GDPs will not adversely affect the Company's financial performance if the supply of SWU from sources other than the GDPs increases, or if demand for SWU, SWU prices, or operating margins decrease by less than the amount set forth under the exceptions to the commitment which would otherwise permit the Company to reduce operations at the GDPs.

Reliance on Nuclear Utility Industry; Customer Concentration

The Company's future prospects in the uranium enrichment business are tied directly to the nuclear utility industry world-wide. Events affecting reactors under contract with the Company or events affecting the industry as a whole, such as business decisions concerning reactors or reactor operations, regulatory actions or changes in regulations by nuclear regulatory bodies, accidents or civic opposition to nuclear operations, could have a material adverse effect on the Company to the extent such events result in the reduction or elimination

of requirements, the suspension or reduction of nuclear reactor operations or cancellation of new nuclear reactor construction.

Domestically, the NRC has temporarily suspended operations at certain reactors due to safety concerns at those reactors over the past year. In addition, business decisions by particular utilities that take into account economic factors, such as the price and availability of alternate fossil fuels, the need for a reactor's generating capacity and the cost of scheduled and unscheduled maintenance and repairs, have resulted in suspended operations or early shutdowns of some reactors and could result in additional suspensions or early shutdowns.

In fiscal 1997, the Company's 10 largest customers represented 50% of revenue and its three largest customers represented 21% of revenue. Nearly all contracts with the Company's utility customers are "requirements" contracts, and a termination or reduction of the nuclear fuel needs of any of the Company's major customers could have an adverse effect on the Company's financial performance. Further, the inability of a major customer to make timely payments could also have an adverse effect on the Company's financial performance. See "Business — Customer Contracts and Pricing."

Competition; Currency Exchange Rates; Trend Toward Lower Pricing

Competition. The uranium enrichment industry is highly competitive. The Company competes with three other major producers: Tenex, a Russian government entity; Eurodif/Cogema ("Eurodif"), a consortium controlled by the French government; and Urenco, a consortium of the British and Dutch governments and private German corporations. See "Industry Overview — Market for Enrichment Services" and "Business — Competition." The Company's competitors may have greater financial resources (including access to below-market financing terms) and receive other types of support from their respective governmental owners which enable such producers to be less cost sensitive. In addition, decisions by foreign producers may be influenced by political and economic policy considerations rather than prevailing market conditions. Further, purchasers in certain areas (particularly Europe and the countries comprising the former Soviet Union) may favor their local producers, due to government influence or national loyalties.

Currency Exchange Rates. The Company's marketing efforts can also be affected by changes in currency exchange rates. Because the Company's costs and contracts are denominated in U.S. dollars, a strong dollar, as has been the case in 1997 and 1998, raises the price of the Company's enrichment services in foreign currencies and weakens the Company's competitive position. Thus, a strengthening of the U.S. dollar against the currencies in which its competitors' costs are denominated could result in the Company lowering its prices to remain competitive, thereby negatively impacting profitability.

Trend Toward Lower Pricing. The Company's profitability over time can be significantly affected by changes in the market price of SWU, which is influenced by numerous factors beyond the Company's control, including such factors as industry overcapacity, excess inventory at customer facilities, global demand, new technologies and production costs of other enrichment suppliers. While there are only a handful of enrichment suppliers, there is an excess of production capacity, and certain suppliers have announced plans to expand their capacities. See "Industry Overview — Market for Enrichment Services." Overcapacity, coupled with sales of buyer-held inventory, and exports of enriched uranium from the countries comprising the former Soviet Union over the last several years have resulted in significant downward pressure on prices. Accordingly, new contracts have significantly lower prices per SWU and have substantially shorter terms than previous DOE contracts, and the Company anticipates that a trend toward somewhat lower prices will continue as the Company competes for new business. There can be no assurance that the Company's financial performance will not be adversely affected by that trend. See "Business — Sales and Marketing" and "Management's Discussion and Analysis of Financial Condition and Results of Operations."

Risks Associated with Purchases Under the Russian HEU Contract

In January 1994, USEC entered into a 20-year contract with Tenex (the "Russian HEU Contract"). See "Business — Russian HEU Contract." Pursuant to the Russian HEU Contract, the Company has ordered 4.4 million SWU, representing 33% of the Company's fiscal 1997 sales, for delivery in calendar 1998, and has committed to order 5.5 million SWU, representing 41% of the Company's fiscal 1997 sales, for delivery in

each of calendar years 1999 through 2001. The Company expects to purchase 5.5 million SWU in each of the years following 2001 during the remaining term of the Russian HEU Contract. As the volume of Russian SWU purchases has increased, the Company has operated the GDPs at lower production levels resulting in higher unit production costs.

The Company's objective is to manage its production and inventory levels taking into account anticipated purchases under the Russian HEU Contract in a manner that most efficiently meets customer demand for enrichment services. A limited number of deliveries by Tenex have been delayed, but they have not disrupted the Company's ability to fill customer orders because of USEC's existing inventory. However, an unanticipated significant delay in deliveries of Russian SWU, or deliveries of SWU not meeting commercial specifications, could require unplanned adjustments to production levels at the GDPs, and adversely impact profitability.

The mechanism for establishing prices for SWU purchases under the Russian HEU Contract through 2001 has been set, and the prices are expected to be substantially higher than the Company's marginal cost of producing SWU at the GDPs. Consequently, although the Company presently can resell the Russian SWU for more than it is paying for the SWU, such sales are less profitable than sales of SWU produced at the GDPs. The effect of this pricing structure will become more pronounced if market prices for SWU decline further, and there can be no assurance that the price the Company pays for the Russian SWU will not exceed the price at which it can resell the material.

Under the terms of a memorandum of agreement (the "Executive Agent MOA") between the Company and the U.S. Department of State and DOE, the Company can be terminated, or resign, as the U.S. Executive Agent, or additional executive agents may be named. In either event, any new executive agent could represent a significant new competitor that could adversely affect the Company's market share and profitability.

Electricity

The GDPs require substantial amounts of electricity (approximately 27.4 million MWhs in fiscal 1997) to enrich uranium, representing up to 59% of the Company's production costs. See "Business — Power." In light of the GDPs' power requirements, an unanticipated interruption to their power supply, including natural or other disasters affecting the generating or transmission facilities which significantly reduces the supply of electricity to the GDPs or an emergency curtailment of electricity, could have a material adverse effect on the Company to the extent it has to curtail operations for any length of time. In addition, to the extent that USEC does not have advance notice of a curtailment of power, the equipment could require significant additional maintenance and result in less efficient operations while being restored.

The Company purchases firm and non-firm power to meet its production needs. The Company's production costs would increase to the extent that the market prices of non-firm power, which represented 37% of the Company's fiscal 1997 power needs, were to rise. In addition, the prices that USEC pays for firm power could increase if there were additional regulatory costs or unanticipated equipment failures at the power plants supplying the firm power to the GDPs. The low-cost power purchase agreements pursuant to which the Company currently purchases firm power expire in 2005. At that time, the contracts are subject to renegotiation, and the price the Company pays for firm power could increase significantly. See "Business — Power."

Upon termination of the power contracts, the Company is responsible for its pro rata share of costs of future decommissioning, shutdown and demolition activities for three coal-fired generating plants. Estimated costs are accrued over the contract period, and the accrued liability amounted to $15.2 million and $12.1 million at June 30, 1997 and 1996, respectively. There can be no assurance that the Company's pro rata share of total costs for such decommissioning and shutdown activities will not exceed the amounts accrued by the Company.

AVLIS

New Technology. There are a number of risks associated with the development and commercialization of AVLIS, a new laser-based uranium enrichment technology (see "Business — Advanced Laser-Based Technology"), and any of these could have a material adverse effect on the Company's financial or competitive position. Additional equipment demonstration and testing activities are necessary before the Company will be in a position to finalize its decision to construct a full-scale commercial facility. The Company could encounter unanticipated delays or expenditures at this stage. If the Company determines not to proceed with AVLIS deployment, the Company would pursue other options for enrichment services such as GDP upgrades or exploring other new technologies, which could have a material adverse effect on the Company's financial or competitive position. In addition, the Company could incur certain additional costs in connection with terminating the AVLIS project, including payments to certain contractors. In the event the Company determines to deploy AVLIS, no assurance can be given that an AVLIS plant could be completed as scheduled or that a full-scale facility will operate at its design capacity.

Based on preliminary design drawings and assumptions regarding the suitability of available sites, AVLIS development and deployment was estimated in September 1997 to cost approximately $2.2 billion from fiscal 1998 through fiscal 2005. The Company periodically re-evaluates its AVLIS estimated costs and currently believes this estimate could vary by up to 20%. If the Company determines to deploy AVLIS, there can be no assurance that development costs or construction costs associated with AVLIS would not be higher than anticipated.

NRC Licensing of AVLIS. The NRC will have regulatory authority over the AVLIS plant and will have to issue a construction and operating license before construction can begin. The NRC will need to develop guidelines for its review of the facility. The development of the guidelines, or the nature and extent of any third-party intervention in the licensing process, could delay or otherwise affect licensing, which, in turn, could delay the commencement of construction. In addition, the NRC would likely require that the Company obtain commercial nuclear liability insurance as a condition to obtaining an NRC license since a commercial AVLIS facility will not be indemnified under the Price-Anderson Amendments Act of 1988 (the "Price-Anderson Act"). There can be no assurance as to the availability, terms or coverage of insurance.

Financing. The Company will require significant financing to achieve commercial deployment of AVLIS. There can be no assurance that financing will be available when required, and the Company cannot predict the cost of or the terms on which such financing would be available.

Intellectual Property. The Company relies on a combination of patent laws, confidentiality procedures and contractual provisions to protect its proprietary information and intellectual property rights related to the AVLIS technology. The Company has received a letter from a third party setting forth such third party's belief that AVLIS will use certain of such third party's technology. See "Business — Advanced Laser-Based Technology — Intellectual Property." In addition, the Company is aware of patents issued to third parties which cover certain technology used in laser-based products; the Company or its licensors may be required to obtain a license to one or more of such patents. There can be no assurance that third party infringement claims will not be brought against the Company in the future, that the Company would not have to pay damages or would not be enjoined in the event any such claims were successful, or that the Company would be able to obtain necessary licenses to certain technology. In the event of such a successful claim of infringement, the Company believes that it can re-engineer the affected apparatus, system or method or obtain any necessary licenses from third parties. However, in the event the Company were unable to successfully re-engineer or obtain from third parties any required licenses at a reasonable cost or at all, a successful claim of infringement could have a material adverse effect on the Company.

International Trade Regulations

The U.S. Department of Commerce and the governments of European countries have imposed duties and other trade restrictions on the quantity of enriched uranium sourced from the countries comprising the Commonwealth of Independent States ("CIS"). While Japan has not imposed formal trade restrictions on CIS-sourced enriched uranium, the general difficulty of Russian products penetrating the Japanese market

has effectively precluded sales into this market by Tenex. Changes in existing trade laws, regulations or relationships could enable Tenex to compete in markets formerly closed to it; increased access by Tenex to these markets could adversely affect the Company's market share and profitability. See "Business — Foreign Trade Matters."

Fluctuations in Financial Results

The Company's financial results fluctuate due to cyclical demand. Deliveries of enriched uranium are determined by customers' reactor refueling schedules which are affected by, among other things, the seasonal nature of electricity demand and the operating availability of the reactor. Utilities try to schedule the shutdown of their reactors for refueling to coincide with periods of low demand, typically during the spring and fall. For efficiency reasons, utilities also attempt to run their reactors for periods of 12 months, 18 months, or in some cases, up to 24 months between refuelings. This variability produces fluctuations in the Company's revenues and earnings quarter-to-quarter, and in some cases, year-to-year related to the timing of sales of SWU. See "Management's Discussion and Analysis of Financial Condition and Results of Operations — Quarterly Financial Information."

NRC Regulation

The GDPs are certified and regulated extensively by the NRC. The Company is subject to an NRC-approved compliance plan (the "Compliance Plan") which requires, among other things, seismic upgrading of two main process buildings at the Paducah GDP. Although the DOE has compensated the Company for expenditures necessary to comply with the Compliance Plan (subject to a maximum amount) by transferring uranium, the Company will nevertheless need to make cash payments for such expenditures. There can be no assurance that expenditures required by the Company to fully comply with the Compliance Plan will not exceed the value of uranium provided by the DOE.

The term of the initial NRC certification expires on December 31, 1998, and the NRC will evaluate the GDPs in connection with the renewal of such certification. In addition, the Privatization Act precludes the NRC from issuing or renewing a license or certificate of compliance if the NRC determines that (i) USEC is owned, controlled or dominated by an alien, a foreign corporation or a foreign government or (ii) the issuance of such a certificate or license would be inimical to the common defense or security of the United States or the maintenance of a reliable and economical domestic source of enrichment services. The NRC has established certain requirements as a result of this statutory directive, including a requirement relating to the financial viability of the Company providing enrichment services. If the NRC were to find that the Company did not comply with the foregoing requirements, it may refuse to issue or renew the Company's certificates, impose certain material conditions, or take other action, which may adversely affect the Company's financial condition. See "Business — Regulatory Oversight."

Environmental Matters

The Company's operations are, and after the Privatization, will continue to be, subject to numerous federal, state and local laws and regulations relating to the protection of health, safety and the environment, including those regulating the emission and discharge into the environment of materials (including radioactive materials). Pursuant to such laws and regulations, the Company is required to hold multiple permits in connection with its operations. The Company has filed for but not yet received permits required for the operation of certain air sources at the GDPs. In addition, certain permits held by the Company require periodic renewal or review of their conditions, and the Company cannot predict whether it will be able to renew such permits or whether material changes in permit conditions will be imposed. Failure to obtain permits or meet any conditions contained therein, or the imposition of additional conditions could have a material adverse effect on the Company's results of operations or financial condition.

The Company incurs substantial costs for matters relating to compliance with environmental laws and regulations including the handling, treatment and disposal of hazardous, low-level radioactive and mixed wastes generated as a result of its operations. Operating costs relating to such environmental compliance

amounted to approximately $24.9 million and $30.4 million for fiscal years 1997 and 1996, respectively, and capital expenditures relating to environmental matters amounted to approximately $1.8 million and $3.5 million for fiscal years 1997 and 1996, respectively. The Company currently estimates that operating costs and capital expenditures for compliance with environmental requirements (exclusive of costs for future disposition of depleted UF_6) will remain at about the same levels in fiscal years 1998 and 1999. Costs accrued for the future treatment and disposal of depleted UF_6 were approximately $72.0 million in fiscal year 1997, which accrual will be eliminated as of the Privatization. The Company expects that costs relating to the future treatment and disposal of depleted UF_6 produced from its operations will be lower in each of fiscal years 1998 and 1999. Due to the possibility of unanticipated events or regulatory developments, however, the amount and timing of future environmental expenditures could vary substantially from those currently anticipated.

The GDPs were operated by DOE and its predecessor agencies for approximately 40 years prior to the Transition Date. As a result of such operation of the GDPs, there are contamination and other potential environmental liabilities. The Company's continued operations may also result in contamination and other potential environmental liabilities. The Paducah GDP has been designated as a Superfund site, and both GDPs are undergoing investigations under the Resource Conservation and Recovery Act ("RCRA"). Although the Privatization Act provides that the U.S. Government remains generally responsible for environmental liabilities arising from operation of the GDPs before the Privatization, the Company is liable for environmental liabilities arising from the Company's operations after the Privatization. See "Business — Environmental."

Natural Uranium Sales

The Company anticipates supplementing its revenues from uranium enrichment services through sales of natural uranium in its inventory and natural uranium transferred to it by the DOE. The quantity of material that USEC will be able to sell in any given year and the revenue generated therefrom will be dependent on market conditions (including any sales by the U.S. Government out of its inventory) and prices at the time, as well as statutory and contractual restrictions on the volume of such sales. While the Company does not anticipate making significant natural uranium sales until after fiscal 2000, there can be no assurance that the Company will be able to sell such natural uranium at anticipated prices and quantities. The failure to complete sales of natural uranium as anticipated could have an adverse effect on the Company's financial condition. See "Business — Natural Uranium and HEU from DOE."

Foreign Ownership Restrictions

The Company's Certificate of Incorporation (the "Charter") sets forth certain restrictions on foreign ownership of securities of the Company, including a provision prohibiting foreign persons (as defined in the Charter) from collectively having beneficial ownership of more than 10% of such voting securities. The Charter also contains certain enforcement mechanisms with respect to the foreign ownership restrictions, including suspension of voting rights, redemption of such Shares and/or the refusal to recognize the transfer of Shares on the record books of the Company. See "Description of Capital Stock — Foreign Ownership Restrictions."

Anti-Takeover Provisions

Under the Privatization Act, no person may acquire, directly or indirectly, beneficial ownership of more than 10% of USEC's voting securities for a three-year period after consummation of the Privatization. The By-Laws establish certain advance notice requirements for the nomination of directors as well as for other stockholder proposals. The Company is also subject to Section 203 of the Delaware General Corporation Law ("DGCL"), which could have the effect of delaying or preventing a change in control of the Company. To the extent that these provisions discourage takeover attempts, they could deprive stockholders of opportunities to realize takeover premiums for their Shares or could depress the market price of the Shares. See "Description of Capital Stock."

Year 2000 Compliance

The Company has been upgrading its date-sensitive software and systems in order to ensure that all software and systems used in its operations will continue to operate without disruption because of Year 2000 issues. However, there can be no assurance that such program will identify and cure all software problems, or that entities on whom the Company relies for certain services integral to its business, such as the power supply, will successfully address all of their software and systems problems in order to operate without disruption in 2000. There can be no assurance that software or system failures or miscalculations causing disruptions of operations or the inability to process transactions will not occur because of the transition from 1999 to 2000.

Absence of Prior Public Trading Market; Possible Volatility of Stock Price

Prior to the Offering, there has been no public market for the Shares, and there can be no assurance that an active trading market will develop or be sustained after the Offering, or that purchasers of Shares will be able to resell their Shares at prices equal to or greater than the offering price. The offering price will be determined by negotiations among the Company, the U.S. Treasury and the Underwriters and may not be indicative of the prices that may prevail after the Offering. For a discussion of the factors considered in determining the offering price, see "Underwriters." Furthermore, the market price of the Shares may be highly volatile. Factors such as announcements of fluctuations in the Company's or its competitors' operating results, events in the nuclear energy industry, and general market conditions for stocks in comparable industries, such as the utility industry, could have a significant impact on the future price of the Shares.

The Company's revenue and operating results can fluctuate significantly from quarter-to-quarter and year-to-year. Customer requirements and, in turn, SWU sale volumes are determined by refueling schedules for nuclear reactors, which generally range from 12 to 24 months, and are affected by, among other things, the seasonal nature of electricity demand, the timing of reactor maintenance and reactors beginning or terminating operations. The Company's cost of sales has been, and will continue to be, adversely affected by amounts paid to purchase SWU under the Russian HEU Contract at prices which are substantially higher than its marginal production cost at the GDPs. In addition, as the volume of Russian SWU purchases has increased, the Company has operated the GDPs at lower production levels resulting in higher unit production costs. Pursuant to the Russian HEU Contract, Russian SWU purchases will peak in calendar year 1999 at 5.5 million SWU per year and are expected to remain at that level thereafter.

Results of Operations For the Nine Months Ended March 31, 1997 and 1998

Revenue. The Company's revenue amounted to $1,056.7 million for the nine months ended March 31, 1998, a decline of $67.7 million (or 6%) from revenue of $1,124.4 million for the corresponding period in fiscal 1997. The decline in revenue was attributable primarily to changes in the timing of customer nuclear reactor refuelings causing a 9% decline in sales of SWU compared with the corresponding period in fiscal 1997. Average SWU prices billed to customers increased approximately 1% compared with the corresponding period of fiscal 1997, notwithstanding the overall trend toward lower prices for contracts negotiated since the Transition Date ("New Contracts") in the highly competitive uranium enrichment market.

Revenue from domestic customers declined $34.9 million or 5%, revenue from customers in Asia increased $36.2 million or 12%, and revenue from customers in Europe and other areas declined $69.0 million or 49%. Changes in the geographic mix of revenue in the first nine months of fiscal 1998 resulted primarily from changes in the timing of customer orders. Sales of uranium to electric utility customers increased to $35.2 million compared with $22.3 million in the corresponding period in fiscal 1997.

Cost of Sales. Cost of sales amounted to $792.2 million for the nine months ended March 31, 1998, a decline of $41.2 million (or 5%) from $833.4 million for the corresponding period in fiscal 1997. The decline in cost of sales was attributable to the 9% decline in sales of SWU from the timing of customer orders, partially offset by the effects of lower production volume and higher unit costs at the GDPs and an increase in purchased SWU under the Russian HEU Contract. As a percentage of revenue, cost of sales amounted to 75% for the nine months ended March 31, 1998, compared with 74% for the corresponding period in fiscal 1997.

In the nine months ended March 31, 1998 and 1997, SWU unit production costs were adversely affected by lower production facility capability, and the Company incurred additional costs because uneconomic overfeeding of uranium was necessary at the Portsmouth GDP to compensate for the production lost due to the unavailability of cells in order to insure that customer requirements would be met. See "Industry Overview — The Enrichment Process — Overfeeding/Underfeeding."

Electric power costs amounted to $316.7 million (representing 53% of production costs) for the nine months ended March 31, 1998, compared with $400.3 million (representing 59% of production costs) in the corresponding period in fiscal 1997, a decline of $83.6 million (or 21%). The decline reflected lower power consumption resulting from lower SWU production and improved power utilization efficiency.

Costs for labor and benefits amounted to $177.9 million for the nine months ended March 31, 1998, an increase of $5.4 million (or 3%) from $172.5 million for the corresponding period in fiscal 1997. The increase reflected general inflation.

Costs for the future disposition of depleted UF_6 amounted to $45.2 million for the nine months ended March 31, 1998, a decline of $14.8 million (or 25%) from $60.0 million for the corresponding period in fiscal 1997. The decline resulted from lower SWU production overall and, at the Paducah GDP, more efficient operations and economic underfeeding of uranium which in turn resulted in a significant reduction in the generation of depleted UF_6. At March 31, 1998, the Company had accrued a total liability of $384.6 million for the future disposal of depleted UF_6.

power to minimize the cost of power per SWU produced. The Company has also adopted cost containment goals intended to be achieved through improved power utilization, increased SWU production per labor hour, and other material and service cost reductions. USEC is committed to containing operating costs while ensuring continued compliance with health, safety and environmental standards.

Commercialize AVLIS Technology. USEC plans to complete the development and commence commercialization of the next generation of uranium enrichment technology, AVLIS, which uses lasers to enrich uranium, and which should permit USEC to remain one of the lowest cost suppliers of uranium enrichment services and enhance its competitive position. The Company believes that it will be able to deploy a full-scale AVLIS facility in 2005. In addition, it is possible that the AVLIS technology may have applications in the medical, precision tool and semiconductor industries which the Company may elect to explore either on its own or through licensing arrangements. As AVLIS is being brought on line for production, the GDP facilities and AVLIS are expected to operate simultaneously. By 2006, AVLIS is expected to be able to displace some or all of the production of the GDPs; however, the Company will evaluate issues such as market demand and other supply sources at that time prior to making any decisions with respect to the GDPs.

Diversify Over the Longer Term. The Company intends to diversify its business over time into related strategic businesses that will contribute to the Company's growth and profitability. This strategy could, among other things, result in the Company becoming involved in other phases of the nuclear fuel cycle that draw on its knowledge of the nuclear industry thereby allowing the Company to become a leader in the global nuclear energy market. Although the Company as a government corporation has not identified any acquisitions or strategic alliances, it intends to pursue appropriate opportunities which, among other criteria, are expected to: (i) offer a favorable balance with respect to market potential and manageable market entry risk; (ii) broaden USEC's operating base beyond its core business in ways that allow for the leveraging of its core competencies; (iii) diversify risk by being counter-cyclical to existing business; (iv) earn returns in excess of certain financial benchmarks including USEC's cost of capital; and (v) be accretive to earnings within a reasonable period of time.

Competitive Advantages

Although the Company operates in a highly competitive environment, USEC believes that the following factors should enable it to compete effectively and continue as the world leader in the uranium enrichment market:

- *Strong Financial Position.* USEC's strong financial position results from a significant backlog of contracted services attributable to established customers and a pro forma balance sheet at March 31, 1998 with $550.0 million in debt (representing 32% of total capitalization, adjusted to include short-term debt). The Company has long-term requirements contracts with utilities to provide uranium enrichment services aggregating approximately $3.2 billion through fiscal 2000 and $7.4 billion through fiscal 2009.
- *Favorable Arrangements with the U.S. Government.* The Company is the beneficiary of several favorable long-term arrangements with the U.S. Government, implemented in connection with the Privatization. These arrangements, which will continue following the Privatization, include:
  - An advantageous lease providing for nominal rent payments for its production facilities with an open term renewal option;
  - Low-cost power purchase arrangements pursuant to which USEC purchases electricity (which represents up to 59% of the Company's production costs) at an average cost of less than 2 cents/kWh; and
  - The assumption by the U.S. Government of substantially all liabilities arising from the operation of the GDPs prior to the Privatization, including substantially all environmental liabilities.
- *AVLIS.* USEC has the exclusive commercial rights to the AVLIS technology developed by the U.S. Government and believes that it has a considerable lead-time advantage over others attempting to develop similar laser-based uranium enrichment technology. The Company believes this new technology has the potential to offer significant cost advantages over both gaseous diffusion and centrifuge

Quarterly Market Report **July 1998**

The Uranium Market Outlook

Market Impact of USEC Inventory Sales

A service of

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1 - Market Impact of USEC Inventory Sales

In the January update of this report, we examined the impact of two different HEU feed supply scenarios on the uranium market using the U-PRICE model. That analysis showed HEU supplies will have a major impact on price, depending on how much feed was made available to the market and how much was taken back by the Russians.

One of the recent major developments in the market is the pending privatization of USEC and the revelation that USEC has substantial inventories of uranium that it plans to sell over the relatively near future, according to its registration statement filed with the Securities and Exchange Commission. USEC plans to sell a greater amount of inventory much sooner than previously thought, and can do this since much of its inventory is not subject to the sales restriction contained in the USEC Privatization Act. These sales levels are also much larger than assumed in the previous analysis of the market, where the impact of different levels of HEU feed supplies was examined.

Because such inventory sales by USEC could have a substantial impact on the market, this report will examine the impact of these sales, again using the U-PRICE model. Instead of adjusting HEU feed supplies as was done in the January study, the present study will look at different levels of USEC (and DOE) sales to determine the likely impact on the market. Since HEU feed supplies are no longer being treated in a parametric fashion, it is necessary to assume a single schedule of their availability to the market. This can now be done with a somewhat greater degree of confidence since additional information is known about the likely availability of these supplies.

Additional developments have occurred during the first half of the year, most of which have negative ramifications for uranium prices. These include economic problems in Asia, which have contributed to lower nuclear growth forecasts and a reduction in inventory holding (which will further reduce market demand there) and deregulation initiatives, especially in the U.S. and Europe, which have also led to lower demand forecasts and reductions in inventory policies, with EDF being the prime example here with respect to inventory reduction. The effects of deregulation have already been felt in the U.S., as several reactors were closed prematurely during 1997. All of these changes must be factored into the analysis as well.

This analysis will proceed as follows. First, we will examine some of the key assumptions used in the analysis, and discuss how they have changed from past assumptions used in similar analyses. In the case of USEC and DOE inventories, we will also specify different rates at which these supplies may become available. Based on these inputs, the impact on price of the different levels of USEC sales, with and without sales by DOE, will be examined. The analysis will conclude with observations on the results generated and their significance for the future uranium market environment.

Assumptions

In this analysis, assumptions are made in a number of areas including uranium requirements, HEU feed supplies, and USEC and DOE sales of uranium stockpiles. These key assumptions are discussed below.

- **Requirements**

One of the key assumptions in any market analysis is the future level of reactor requirements. Recently, requirements have been negatively affected by deregulation and the economic problems in the Far East. These impacts have been captured in a recent forecast by the U.S. Energy Information Administration (EIA). Figure 1 compares EIA's Western World forecasts as of 1997 and 1998, and shows that beyond the year 2007, EIA's new requirements forecast is generally 5-10 million pounds U_3O_8 per year lower than its 1997 forecast. Much of this decrease occurs in the Far East, where lower growth of nuclear power (and requirements) is forecast, as shown in Figure 2.

Figure 1. EIA Requirements Forecasts for Western World as of 1997 and 1998

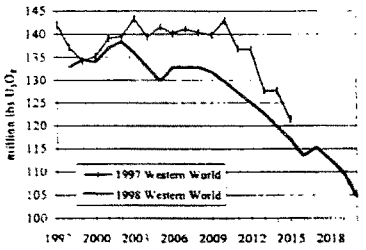
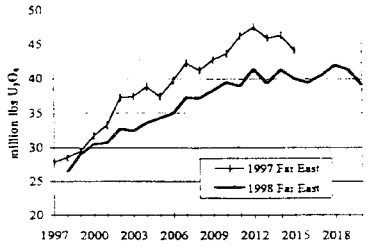
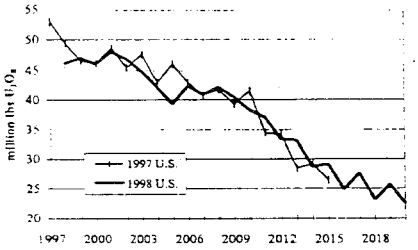


Figure 2. Comparison of 1997 and 1998 EIA Forecasts for Far East



EIA forecasts of U.S. uranium requirements exhibit little change between 1997 and 1998 (Figure 3), although they continue to show a steady degradation over time, falling to 25 million pounds by 2016.

Figure 3. Comparison of 1997 and 1998 EIA Forecasts for the United States



EIA's most recent reference case is used as the requirements input for this analysis. While this case is somewhat lower than Ux's low case, it represents the most recently published requirements forecast, and thus reflects developments that have taken place recently.

- **HEU Feed Supplies**

The present analysis assumes that the Russians take back approximately one-third of the feed contained in the HEU, with shipments back to Russia beginning next year (Figure 4). Initially, sales are much less than available supply, due to trade and legislative restrictions, and thus inventories of HEU feed are built up, as shown in Figure 5. Sales ramp up as the U.S. quota increases; the Russians are also able to sell more outside the U.S. as non-U.S. unfilled demands grow. Eventually, sales exceed the amount of HEU feed retained in the U.S. and feed inventories are drawn down until they are exhausted. After this point, sales match HEU feed deliveries net of what is returned to Russia. The assumption is that the Russians will want to sell feed inventories as soon as practicable in order to generate revenues.

Figure 4. HEU Feed Supplies and Russian Take-Back of Feed, 1998-2010

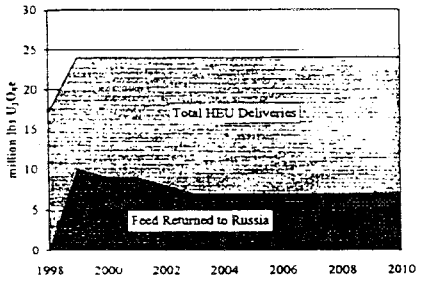


Figure 5 Assumed HEU Feed Sales vs. U.S. Retained Supplies and Inventories

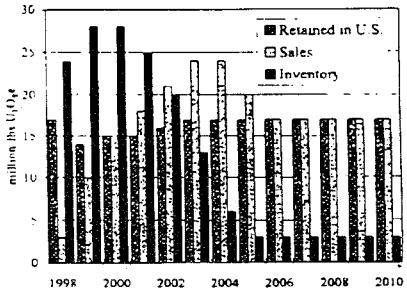
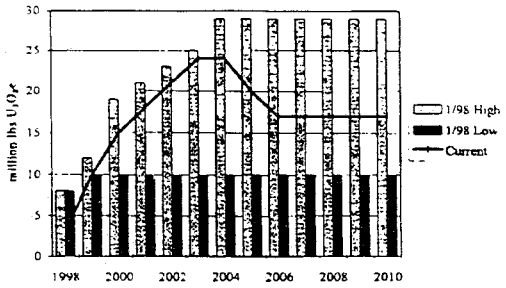


Figure 6 compares this current schedule of HEU sales with the high and low cases assumed in the January study. This comparison shows that the current case is much closer to the earlier high case in the initial years, but out past the year 2004 it falls in the middle of the high and low cases, gravitating to the low case in the out years. The January high case assumed that no material was returned to Russia and that feed inventories were not worked down until 2010. While inventories do not build to as large a level in the current case, the assumption is that these inventories are worked off by 2005, and sales after that match the lower net receipts of feed.

Figure 6. Comparison of Current HEU Sales Assumption with 1/98 High/Low Scenarios



- **USEC Sales**

USEC's inventories include those currently in hand and those scheduled to be transferred to it by DOE. Inventories to be transferred to USEC include 7,000 MTU as UF_6 and 50 MT of HEU as called for in the USEC Privatization Act, and about 11 million pounds U_3O_8 as UF_6 as payment for safety upgrade work at the gaseous diffusion plants. USEC also received uranium from DOE at the time of its formation as well as a transfer of 13 MT HEU as UF_6 which is currently being blended down at Portsmouth. In all, USEC inventories total almost 75 million pounds U_3O_8 in the form of UF_6, both natural and enriched. These inventories are listed in Table 1

Table 1. USEC Uranium Inventory and Expected Transfers

	thousand kgU as UF_6	thousand lbs U_3O_8e
Inventories at March 31, 1998	12,145	31,577
Transfer of 45 metric tons of LEU	453	1,178
Transfer of 3,800 metric tons of uranium	3,800	9,880
Transfer of 0.8 metric tons of HEU	211	549
Transfer of 7,000 metric tons of uranium	7,000	18,200
Transfer of 50 metric tons of HEU	5,000	13,000
Total:	**28,609**	**74,383**

Source: USEC Inc. S-1 registration statement.

According to its registration statement, USEC plans to sell over 60 million pounds of these inventories by the end of 2005. This is about double the 31 million pounds U_3O_8e that is scheduled to be transferred to USEC according to the USEC Privatization Act. The resale of material transferred pursuant to the Act is limited to 3.1 million pounds per year, but the remainder of USEC's inventory has no resale limits. In line with its registration statement and other information that has become available, it is assumed that USEC will sell the feed according the schedule labeled "USEC Sales" in Table 2

Table 2. Availability of Inventory Supplies by Source, 1998-2010

Source	1998	1999	2000	2001	2002	2003	2004	2005	2006	2007	2008	2009	2010
[illegible]	3,000	5,100	10,500	13,400	18,100	11,300	3,400	0	0	0	0	0	0
[illegible]	0	3,000	5,000	5,000	6,000	4,000	2,000	1,000	0	0	0	0	0
DOE	1,000	1,000	2,000	3,000	6,000	6,100	4,000	5,000	6,000	1,500	1,500	1,500	1,500
Total	4,000	9,100	17,500	21,400	30,100	21,300	9,400	6,000	6,000	1,500	1,500	1,500	1,500

In its registration statement, USEC notes the "economic underfeeding of uranium which in turn resulted in a significant reduction in the generation of depleted UF_6." USEC would have additional inventory to sell if it were to operate its gaseous diffusion plants in an underfeeding mode in the future, since when the plants are

"underfed" they are operated at a lower tails assay than the average tails assay on which feed deliveries by USEC's customers are based, resulting in a buildup of inventory. By operating the plants in this manner, information suggests that USEC could generate an additional 28 million pounds of supply over the period being examined. This supply would be made available to the market on the schedule labeled "Underfeeding" in Table 2.

- **DOE Sales**

DOE's inventories come from a number of sources, including natural UF_6 stockpiles and off-spec HEU which is to be blended down for use at TVA. In addition, DOE has about 7-8 million pounds U_3O_8 as UF_6 of Russian HEU feed. This is the balance of the feed associated with the first two years of deliveries made by the Russians, where the feed was paid for by the U.S. government and part of it was repurchased by the Russians for use in the matched sales program permitted under the Russian suspension agreement. Further, DOE has inventories located at its field offices. Some of these inventories could be made readily available to the market, while some would need to be processed further before they could be made available.

In the analysis below, it is initially assumed that DOE will not sell any inventory, so the net impact of the two scenarios for USEC sales—with and without underfeeding—can be determined. Then DOE sales are added at the rate assumed in the schedule shown in Table 2.

Results

To investigate the degree to which inventory sales by USEC could impact price, a base case is developed which includes no sales by either USEC or DOE, but where Russian HEU feed is introduced at the rate shown in Figure 6. That base case is illustrated in Figure 7. In the case where there are no USEC and DOE sales, the spot price would stay above $11/lb for the period of the study. Sales by USEC of 60+ million pounds at the rate assumed in Table 2 would push price down to almost $8/lb in the year 2000, when the difference between the two cases is over $3.00. This reduction in price from the base case and its current level of $10.50/lb is understandable when one considers the amount of inventory that it is assumed to be sold then versus what has already been placed in 2000 or such sales today. USEC is assumed to sell 10.5 million pounds in 2000, an amount in addition to the 11 million pounds the Russians are assumed to sell in the base case, meaning that between them, there would be inventory sales of 21.5 million pounds, the vast majority of which has not been placed

Figure 7. Impact of USEC Sales on Uranium Prices, 1998-2008

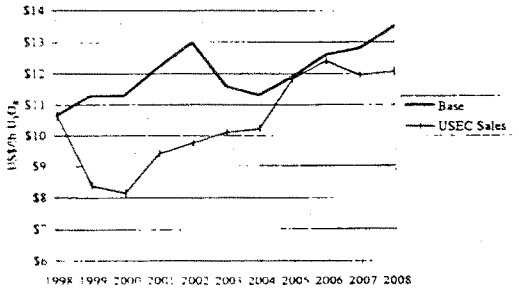
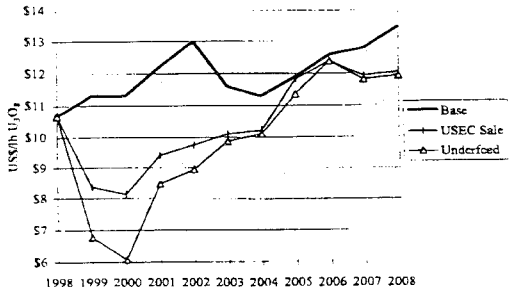


Figure 8 shows that additional USEC sales resulting from operating the enrichment plants in an underfeeding mode to yield the supplies assumed in Table 2 would push price down further, to $6.00/lb in 2000, when USEC would sell 15.5 million pounds, and USEC sales and Russian HEU feed together would total 26.5 million pounds

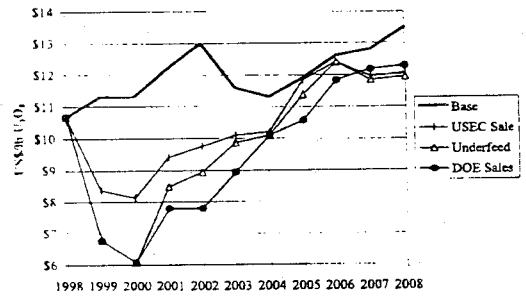
Figure 8. Impact of USEC Underfeeding in Addition to USEC Sales, 1998-2008



- **DOE Sales**

Adding DOE sales in the amounts assumed in Table 2 would depress prices further, as shown in Figure 9 which examines the combined effect of USEC and DOE sales on the market. In this case, after falling, the spot price stays below $8.00/lb until 2003

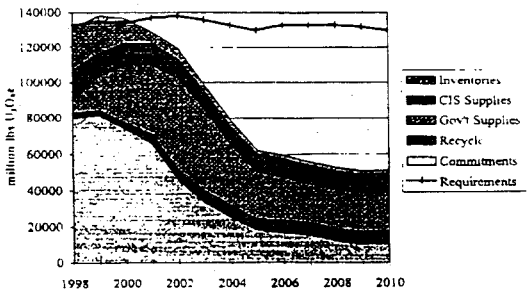
Figure 9. Impact of DOE Sales in Addition to those by USEC, 1998-2008



The reason that price is pushed to such low levels in the near term is due to the limited market demand that is available in those years, given current contract commitments and the availability of inventory supplies. This situation is illustrated in Figure 10, which compares Western uranium requirements against utility inventory usage,

assumed CIS supplies to the West, assumed government inventories (which include Russian HEU feed sales from Figure 6 and total sales by USEC and DOE as shown in Table 2), planned recycle of plutonium, and current contract commitments. As shown, not only is there no uncommitted demand left in 1999 and 2000, but supplies exceed requirements. Of course, this oversupply is much worse than shown because of the uncommitted mine production that is not included in the figure. This near-term supply/demand imbalance is what causes extreme downward pressure on price.

Figure 10. Western World Requirements vs. Supply Sources, 1998-2010



Additional Observations and Conclusions

This analysis assumes that both USEC and DOE are price-takers, in that they will sell the amounts assumed irrespective of the prices received. In reality, it may be the case that they alter their sales levels, so as not to impact price as severely. In principle, USEC should try to maximize profits on uranium sales. However, to the extent that USEC enrichment revenues decline, USEC may need to sell uranium to maintain its market share for enrichment and generate cash flow, or to pay promised dividends. As a government organization, DOE's actions would be more subject to political pressure, and decisions may be made not to sell when prices are depressed. Such pressure appears to have been a factor in keeping DOE from selling more than it has to date.

Even if USEC were to refrain from selling due to the negative impact this action would have on price, it does not necessarily follow that low prices would not materialize. Other suppliers, sensing that USEC has these inventories to sell, could try to beat USEC to the market, and this preemptive selling activity would serve to push price down. The key point is that the ultimate market outcome not only depends on how USEC acts, but also on how other suppliers react to USEC's sales potential.

This type of preemptive selling could also apply to the Russians and their HEU feed, although they face restrictions on how much they can sell. There is also the possibility, which cannot be overlooked, that sharply reduced uranium market prospects would cause the Russians to break off the HEU deal. Although this scenario is not examined here, it would have a sharply positive impact on price.

This analysis does not differentiate between whether the Russian HEU feed sales are made by Western uranium producers, the Russians themselves, or a combination of the two. To the extent that these sales were made primarily by Western producers who could sell under existing contracts and cut back production to accommodate these supplies, prices would be higher than shown here. However, the prospect of lower prices over a long period of time suggested in this analysis means that producers would be unlikely to purchase the Russian HEU feed, and thus this stabilizing factor would not be present in the market.

Further, this analysis does not take into account the fact that most of the Russian HEU feed and USEC and DOE sales will be made into the U.S. market, but instead looks at supply and demand from a Western world perspective. In reality, these supplies cannot be readily sold to certain geographic markets, particularly Western Europe where the attachment of U.S. nonproliferation obligations makes them less attractive. Thus, the oversupply situation in the U.S. due to the sale of these supplies is likely to be actually greater than for the Western world as a whole.

USEC now has significantly more inventory to sell than previously assumed by the industry and in analyses by UxC and others. Further, it is apparent that USEC wants to sell this material within a relatively short time frame. USEC may be making these

pronouncements to make its stock appear more attractive, although this analysis has shown that, coupled with the assumed rate of sales of Russian HEU feed, USEC sales would push price well below current levels.

In addition to USEC now having more inventory it wants to place, the prospects for the uranium market are worse now than at the time the USEC Privatization Act was passed. In this regard, the Russians and USEC/DOE are competing for a market that is now smaller and more price sensitive than the one that existed when the Russian HEU feed sales quota was first devised. As a result, USEC and Russia cannot both expect to sell uranium in the quantities desired without a devastating impact on price. In short, there is not enough room in the market for both Russia and USEC.

ORIGINAL

UNITED STATES ENRICHMENT CORPORATION

- - -

FORTY-NINTH MEETING

OF THE BOARD OF DIRECTORS

- - -

Third Floor Conference Room

USEC Headquarters

6903 Rockledge Drive

Bethesda, Maryland

Wednesday, July 22, 1998

BOARD MEMBERS PRESENT:

WILLIAM J. RAINER, Chairman, presiding

WILLIAM BURTON

CHRISTOPHER COBURN*

MARGARET H. GREENE

DR. KNEELAND J. YOUNGBLOOD

OFFICERS PRESENT:

ROBERT J. MOORE, General Counsel

business expenses, but any -- in other words -- let me step back on that. It was clarified to state that one-time payments that were special, non-everyday business expenses, would not be included in USEC's calculation under this agreement of operating margin.

On that basis, unless the business itself goes completely into the tank, it is very unlikely in any scenario that's been projected that that 10 percent will be breached. As the letter that you have, that the Chairman and the CEO sent on July 10th, states, there would have to be a decline of over 40 percent in earnings before you'd even begin to get close, and nothing in our current projections even comes close to that.

The second issue was the falling of new contracts below $80 per SWU. The intent at the time it was agreed to was not the very next contract you signed. This became a major issue because there was some concern that, as you all know, the prices have been falling and the average price of new contracts has been heading below $90. There was some concern stated in the press it would be as low as 85, 84, the $80 would be breached within the next year.

This was clarified to state what was originally intended, and indeed one could have read it that way, but you could also have read it otherwise. So this letter

that goes beyond these two points. If there is, they haven't stated it to us or said it to a newspaper.

MR. BURTON: But you know, they did ask to come speak today and we could ask them that question if we had said yes. I just -- I don't understand why we have some aversion to receiving information other than from the financial advisers. I just don't understand that.

CHAIRMAN RAINER: Have we already heard from them?

MR. BURTON: On this particular issue? I can't recall.

CHAIRMAN RAINER: We heard them for an hour when they asked to come here the last time.

MR. GOLDMAN: I think the decision related to this being pricing, and I also think it related to the fact that they had been given this information, but they continued to complain without giving a reason. That's all we know.

MR. BURTON: Well, but --

CHAIRMAN RAINER: What, Bill -- I take this very seriously. What do they add to your determination about the commitment to operate the GDP's? What is it that changes from the last meeting in your opinion that all of a sudden the IPO does not qualify for meeting the commitment test? What possibly could the labor union say

MR. DERRYBERRY: Chris?

CHAIRMAN RAINER: Chris Coburn? Chris said he had to go to his meeting, he said at 2:00, so I assume that's where he is.

MR. RYAN: What's your schedule, Bill?

CHAIRMAN RAINER: My schedule was to be finished with this 30 minutes ago, so I'm behind schedule. I'm hoping that we'll be in a position to listen to Morgan Stanley's preliminary price talk not later than 3:00 o'clock. It looks to me like we have one more issue, some uranium issues and Russian HEU, to thrash out. The other topics it seems to me are not particularly contentious, but we'll wait and see.

Now, this goes to the national security question, which again before the meeting Bill asked some people to go over. And in sympathy to that and I thought it was a good idea, I've asked Les to summarize the events that have happened recently. This has been a very tricky one, but we're pleased with where we are right now.

MR. GOLDMAN: Another development in the intervening period has been concerns, expressed primarily by the academics who have been associated with the Russian HEU agreement from the beginning, that the amount of inventory of natural uranium which USEC was holding was going to cause market-oriented problems in terms of the

meeting. He wanted me to know that we all know that this is not a new topic, so it is a renewed focus on this topic recently; and that we should know that in the last several days countless hours have been taken by senior members of this administration to take a look at the issues that have been raised; and that we should be confident that everyone in the administration is planning on pricing this IPO this afternoon.

So there is a derivative conclusion from that.

MR. BURTON: I have a couple questions on this and a comment. Mr. Chairman, I had asked specifically for two different presentations on this because I think this is such a critical issue. I had asked for the Congressional members that had expressed a concern -- I was thinking specifically of Senator Domenici, chairman of the Senate Budget Committee, Subcommittee chairman of the Water and Energy on the Appropriations, who has expressed serious concerns about it -- to speak. I was told that might inflame the market and so they wouldn't be invited.

I also asked that a National Security Council or other security person to speak to us. Les' presentation was helpful, but certainly doesn't sub for that.

I was offered a pre-meeting briefing by Gary Gensler, which he delegated to one of his staff members, who on several occasions mentioned: Well, this is third-

resolution before we move to a vote?

MR. BURTON: Real briefly, and I mean that. The reason I'm not in a position to vote on it at this point is in the first paragraph, subparts (a)(1), which is "whether the privatization will result in a return" -- I'm sorry, not (a)(1). (a)(3), "not be inimical to the health and safety of the public, the common defense," and then (b)(3), which talks about ensuring that we have a reliable and economical domestic source of uranium mining.

I don't think we have enough information in light of this issue that has risen up. There has been a ton of press, a ton of meetings, everybody who's been involved in it except this Board, and we can't even get a briefing on them.

So I don't have enough information on those two topics to know whether the change that's occurred since we voted is of a material way that should affect it. Finally, I just have a hard time voting that it does secure the maximum proceeds until I hear the price.

So I'm going to have to abstain.

CHAIRMAN RAINER: Youngblood?

DR. YOUNGBLOOD: In favor.

CHAIRMAN RAINER: Rainer is a yes.

Greene?

MRS. GREENE: Yes.

TED STRICKLAND
6TH DISTRICT, OHIO

COMMITTEE ON COMMERCE

SUBCOMMITTEE ON ENERGY AND POWER

SUBCOMMITTEE ON OVERSIGHT AND INVESTIGATIONS

SUBCOMMITTEE ON HEALTH AND THE ENVIRONMENT

Congress of the United States
House of Representatives
Washington, DC 20515–3506

RURAL HEALTH CARE COALITION

OLDER AMERICANS CAUCUS

EDUCATION CAUCUS

STEEL CAUCUS

MINING CAUCUS

CORRECTIONAL OFFICERS CAUCUS
FOUNDER AND CO-CHAIR

July 20, 1999

The Honorable Richard Lugar
Chair
U.S. Senate Committee on Agriculture, Nutrition and Forestry
Washington, DC 20510

The Honorable Tom Harkin
Ranking Minority Member
U.S. Senate Committee on Agriculture, Nutrition and Forestry
Washington, DC 20510

Dear Chairman Lugar and Ranking Minority Member Harkin:

I am writing to provide you with information regarding Mr. William J. Rainer's conduct as Chairman of the United States Enrichment Corporation's (USEC) Board during the privatization of the Department of Energy's (DOE) uranium enrichment plants last summer. As Chairman of the USEC Board, Mr. Rainer was authorized, with the approval of the Secretary of the Treasury, to "transfer the interest of the United States in the United States Enrichment Corporation to the private sector..." (USEC Privatization Act, P.L. 104-134, Section 3103) As you may know, one of USEC's uranium enrichment plants is located in my district in Piketon, Ohio and I would like to take this opportunity to share with you some of my serious reservations about Mr. Rainer's qualifications for the Commodity Futures Trading Commission (CFTC) given his actions during the privatization of USEC.

Under the Energy Policy Act of 1992, the government-owned corporation, USEC, was created to assume responsibility for the DOE's uranium enrichment program. The Act not only transferred the Department's uranium enrichment program to USEC, but it also included a requirement that USEC prepare a strategic plan to privatize the corporation. On July 28, 1998, USEC was privatized in a public offering of stock. On more than one occasion, I raised concerns that the privatization of the uranium industry would result in a conflict of interest between the private company and the statutory criteria established by Congress to direct the sale of USEC. This inherent conflict would unnecessarily place at risk an important foreign policy measure, namely the U.S. - Russia Highly Enriched Uranium (HEU) Agreement.

First, let me describe the statutory criteria provided to guide the Board's decision making during the privatization process. Specifically, the eight statutory criteria called for the following: 1) Net present value of the corporation: privatization will result in a return to the U.S. at least equal to

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(740) 286-664

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MARIETTA, OH 45750
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the net present value of the corporation; 2) No foreign control: privatization will not result in the corporation being owned, controlled, or dominated by an alien, a foreign corporation, or a foreign government; 3) Protecting public heath and national security: privatization will not be inimical to the health and safety of the public or the common defense and security; 4) Assuring domestic uranium enrichment capacity: privatization will provide reasonable assurance that adequate enrichment capacity will remain available to meet the demands of the domestic electric utility industry; 5) Long-term viability of the corporation.; 6) Operation of the Gaseous Diffusion Plants: privatization will provide for the continuation by the Corporation of the operation of the DOE's Gaseous Diffusion Plants; 7) Reliable and economic nuclear fuel industry: privatization will provide for the protection of the public interest in maintaining a reliable and economic domestic source of uranium mining, enrichment, and conversion services; and 8) Maximizing proceeds from privatization: to the extent not inconsistent with requirement 5 through 7, privatization will secure the maximum proceeds to the U.S. (See USEC Summary of Statutory Requirements and April 29, 1998 letter)

In 1993, the United States and the Russian Federation entered into an agreement to ensure that highly enriched uranium from dismantled nuclear warheads would be used for peaceful purposes only. In January 1994, President Clinton announced that the U.S. had signed a contract with Russia to purchase $12 billion of highly enriched uranium over a 20-year period. The U.S. purchase of 500 metric tons of this material is clearly a crucial national security initiative. This foreign policy measure provides an important incentive to the Russian Federation to continue dismantling its nuclear weapons and ultimately helps to safeguard the U.S. and the rest of the world from the threat of a nuclear incident.

One of my greatest concerns regarding privatization was that USEC's role as Executive Agent for the U.S. under the HEU Agreement would jeopardize the HEU Agreement or lead to a business decision that would result in the closure of one of the two gaseous diffusion plants. The public objective of purchasing specific quantities of Russian uranium and the corporation's goal to maximize profits directly conflict with each other. I still fear that private business objectives would overshadow national security and energy security which ultimately leads to violations of the statutory requirements outlined in the Energy Policy Act of 1992 and the 1996 Privatization Act, listed above.

On July 1, 1999 USEC made available the transcripts from the four Board meetings immediately preceding the privatization of the corporation. These transcripts confirm that Mr. Rainer's conduct compromised the Congressional mandate that privatization should not be inimical to the national security. In fact, the transcripts show that a Board member inquires about a letter from Senator Domenici, June 26, 1999, (attached) which raises concerns "that a privatized executive agent can still function in the way necessary to carry out the national security objectives of the HEU Agreement." The Board member's interest in having Senator Domenici brief the Board on his concerns was denied because it "might inflame the market." (July 22, 1998 Transcripts, page 53) According to the transcripts, *Mr. Rainer placed the need to move forward on privatization immediately over the request of other Board members to receive a briefing from Senator Domenici or the National Security Council on national security developments.* Instead, Mr. Rainer accepted a second-hand response to the Board member's questions about national security implications.

I must underscore that shortly after the privatization of USEC, Russia suspended shipments of enriched uranium due to the impacts of privatization -- namely because of the fact that USEC entered the private market with 30 million more pounds of government uranium than was assumed when the 1996 USEC Privatization Act was adopted. Ultimately, $325 million was included in the Fiscal Year 1999 Omnibus Appropriations Act for the purchase of two years worth of natural uranium under the Russian Agreement. This confirmed my suspicions that privatization of this industry would weaken the U.S.-Russia HEU Agreement, threaten national security, violate the congressional mandates, and ultimately force the government to commit millions, if not billions, of dollars to bailout the privatization deal.

Despite the discussions during the July 22, 1998 USEC Board meeting and the close vote on the final decision to privatize (3-in favor of privatization by an initial public offering, 1-against and one abstaining), it is my understanding the full Board was never briefed by Senator Domenici, NSC, or even outside experts such as Tom Neff, the MIT physicist who has been credited with conceiving this non proliferation agreement; Richard Falkenrath, a national security scholar at Harvard who publicly shared his reservations about the privatization of USEC; or Joseph Stiglitz, former Chairman of the Council of Economic Advisors who also publicly raised concerns about the decision to privatize the uranium enrichment industry. I find this blatant disregard for national security concerns by Mr. Rainer, as the Chairman of the USEC Board, to be disturbing and alarming. However, this behavior does not surprise me given Mr. Rainer's apparent determination to privatize this industry.

I had a private meeting with Mr. Rainer last Spring and during that meeting I stated that I thought it was likely that USEC would be sold through a public offering rather than acquired by a private company. He asked me why I thought that and I explained that I felt it was in the best interest of the current management team if the industry were sold through a public offering -- this method of transferring the public asset to the private sector would allow the presiding officers to keep their positions at a considerable financial gain whereas an acquisition would not assure them employment with the private corporation. Mr. Rainer firmly stated that this was not the case and that the current CEO and management team would have no major influence in the decision-making process for determining the method used to privatize USEC.

On May 22, 1998, I sent a FOIA request to the Department of Treasury and Senators Glenn and DeWine and Representative Whitfield joined me in a second letter dated July 8, 1998, asking for documents and information to which we thought the public should have access. In response to that request, I received a number of documents. Those documents included a letter from Chairman Rainer to USEC's CEO, Nick Timbers, and other officers of the corporation waiving the prohibition of 18 U.S.C. §208(a) which provides criminal penalties where a government official or employee participates in a matter in which he/she has a substantial financial interest. The letter written on September 26, 1995, stated that these employees' financial interest in the privatization of USEC "is not so substantial as to be deemed likely to affect the integrity of the services which the Government may expect from the employee." (see attached September 26, 1995 letter) Mr. Rainer had signed this letter nearly three years before he sat in my office and denied that Mr. Timbers and others would have significant influence over the USEC privatization decision.

The issuance of these waiver letters is particularly interesting in light of the fact that I have recently had the opportunity to review the transcripts from the USEC Board meetings which occurred in the month and a half prior to the sale of the industry. *The personal guarantee that I received from Mr. Rainer during our meeting, that the current management team would not play a dominant role in the privatization decision making process, was clearly not fulfilled. In the transcripts, Mr. Timbers, clearly and forcefully argues for the public offering approach to privatization. (See June 3, 1998, page 268) I am greatly troubled by the fact that Mr. Rainer behaved in a manner which led me and my colleagues to believe that the present management team of USEC would not participate significantly in the decision making process during privatization, yet indeed they did. Furthermore, I cannot overstate the lack of trust I have in Mr. Rainer. He told me that Mr. Timbers would not play an pivotal role in the privatization decision making process, yet at that time, he knew he had signed a waiver for Mr. Timbers to do exactly that.*

I believe that Mr. Rainer's conduct during privatization raises questions about whether or not Congressional intent was followed and whether the process was managed in a manner which allowed for fair competition (June 3, 1998 transcripts, page 198). I have serious reservations about the integrity of the USEC privatization process because the current management team was afforded the opportunity to advise the USEC Board on its competitors bids and the process was conducted without appropriate public access to information. In fact, I did not receive these transcripts until nearly a year after the process was over. And finally, the 1992 Energy Policy Act and the 1996 USEC Privatization Act quite clearly outline eight statutory criteria which were to be the framework for making the decision to privatize. I am not confident that Mr. Rainer met his public responsibilities as the authorized officer to transfer this important government asset to the private sector.

I have shared with you only some of my concerns regarding Mr. Rainer's conduct during the privatization of USEC. I feel it is my duty to alert you to some of the troubling circumstances and decisions leading to the privatization of USEC, and I have enclosed the transcripts I referenced as well as other documents I think might be helpful to you as you review the issues I have raised.

Thank you for your consideration of this important matter and if you have any questions, please do not hesitate to contact me at 202-225-5705.

Sincerely,

Ted Strickland

Ted Strickland
Member of Congress

cc: The Honorable Mike DeWine
The Honorable George Voinovich

The Secretary of Energy
Washington, DC 20585

October 22, 1999

MEMORANDUM FOR JOHN PODESTA
CHIEF OF STAFF TO THE PRESIDENT

FROM Bill Richardson

SUBJECT USEC's Request for Federal Assistance

USEC is asking the Administration for its support for a direct appropriation to cover losses it is incurring due to low market prices under its U.S.-Russia HEU agreement. I have very strong views about our domestic equities that USEC has not addressed.

First, USEC is informing Administration and Capitol Hill officials that it will terminate its role as Executive Agent of the HEU agreement on December 1st, if it does not receive federal assistance. Capitol Hill is being told that USEC has the support of the NSC and State Department for $200 million in assistance.

Second, citing the end of its employment agreement obligations with the United States made upon privatization, USEC plans substantial layoffs at the Gaseous Diffusion Plants at Portsmouth, Ohio and Paducah, Kentucky in July, 2000, which could affect as many as 1,500 workers of the 3,200 workforce. (There are also rumors that USEC may close the Portsmouth facility.) DOE has asked USEC to inform us of their plans and to work with us on an orderly transition – so far, to no avail.

Finally, FY 2000 appropriations enacted for DOE do not provide adequate funds for several of the Administration's most critical priorities, thus, DOE cannot afford an offset to fund USEC's request for federal assistance. Other funding sources need to be found.

Should the Administration determine that USEC's agency is central to the success of our HEU agreement with the Russians, I would insist that stringent contingencies be placed on any assistance provided, and that the lion's share of that assistance be used to mitigate the serious employment and safety concerns at the Gaseous Diffusion Plant sites in the United States.

Please keep me apprised of any developments on this issue. As always, I appreciate your consideration and look forward to working with you.

GEORGE V. VOINOVICH
OHIO

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GOVERNMENTAL AFFAIRS
CHAIRMAN, SUBCOMMITTEE ON OVERSIGHT OF GOVERNMENT MANAGEMENT, RESTRUCTURING AND THE DISTRICT OF COLUMBIA
ENVIRONMENT AND PUBLIC WORKS
CHAIRMAN, SUBCOMMITTEE ON TRANSPORTATION AND INFRASTRUCTURE
SMALL BUSINESS
ETHICS

January 26, 2000

William H. Timbers
President and Chief Executive Officer
United States Enrichment Corporation
6903 Rockledge Drive
Bethesda, Maryland 20817

Dear Nick

We are writing with concerns regarding the recent reports of the potential plant closure of either of the Gaseous Diffusion Plants (GDP), currently being operated by USEC in Portsmouth, Ohio and Paducah, Kentucky.

In July, 1998, when USEC was privatized in the largest ever privatization of a federal corporation, USEC entered into the Agreement Regarding Post-Closing Conduct with the Department of Treasury acting on behalf of the United States Government. This Agreement requires continued operation of both plants through 2004 unless one of four Significant Events occur. These four events, as outlined in the Agreement, will exempt USEC from continued operation at either plant. According to the Department of Treasury, USEC indicated on Form 10-Q, filed on November 5, 1999, that "[n]one of the [Significant Events] to USEC's obligation to operate the plants has occurred."

However, recently, it has been indicated to our staffs that USEC anticipates plant closure at either the Portsmouth or Paducah Plant to occur sooner than 2004. We understand that the USEC Board of Directors, in a meeting on January 25, 2000, discussed the possibility of plant closure and that these discussions will continue next week.

We would like to remind you of several statements made by you and Mr. William J. Ranier, former Chairman of the Board of Directors for USEC, prior to privatization. On April 24,1997, you wrote Mr. Robert Wages, President of the then Oil, Chemical and Atomic Workers Union, about perceived misunderstandings by the union. In that letter, you stated that "all operating plans considered by USEC require the running of both GDPs until the year 2004." On May 1, 1998, right before privatization, Mr. Ranier corresponded with Mr. Wages and restated and referenced the position in your April 27, 1997 letter that USEC remained committed to operating both plants until 2004.

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37 WEST BROAD STREET
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At the same time, the union was expressing concern about the effect the United States-Russian Highly Enriched Uranium (HEU) Agreement and USEC's position as Executive Agent would have on continued long-term operations at both plants. The union shared these concerns with Vice President Al Gore, who, on May 22, 1998, replied that USEC would be required to enter into binding agreements to continue operation of both plants for a reasonable period of time. It is our belief that the eighteen months that have passed since privatization do not constitute a reasonable period of time for continued operations.

Finally, the 1996 USEC Privatization Act requires the continued operation of the two facilities and that a reliable domestic supply of uranium mining, enrichment services and conversion services are maintained. At this time, USEC supplies only seventy-five percent of the domestic market share for enriched uranium. Of this seventy-five percent, approximately half of this supply is derived from the Russian HEU Agreement.

Now, we are forced to question whether USEC entered into the Agreement on Post-Closing Conduct in good faith. It appears to us because of USEC's current consideration of plant closure, whether it is Portsmouth or Paducah, that USEC entered into the agreement without fully considering the effects that market supply would have on our country's enrichment activities.

We expect that you will fulfill your past promises and the Agreement on Post-Closing Conduct and continue operation at both plants until at least January 1, 2005.

These uranium enrichment plants perform a critical role in providing for the energy security of this nation. We must stress that thousands of Ohio and Kentucky families depend on your corporation for their livelihood and that a closure of either facility would have a devastating impact on the local economies.

We thank you for your personal attention to this matter.

Sincerely,

George V. Voinovich
United States Senator

Mike DeWine
United States Senator

Ted Strickland
United States Representative

DEPARTMENT OF THE TREASURY
WASHINGTON, D.C.

UNDER SECRETARY

January 31, 2000

Mr. William H. Timbers, Jr.
President and Chief Executive Officer
USEC Inc.
Two Democracy Center
6903 Rockledge Drive
Bethesda, MD 20817-1818

Dear Mr. Timbers:

We have been informed that the Board of Directors of USEC Inc. may be about to consider the closure of one of USEC Inc.'s gaseous diffusion plants. As you know, the Agreement Regarding Post-Closing Conduct dated July 14, 1998 (the "Agreement"), which was signed by USEC and the Treasury Department prior to privatization, directly addresses the issue of plant closings. Specifically, the Agreement permits a USEC plant closing before January 1, 2005 only "if a Significant Event has occurred with respect to such Plant." The Agreement clearly defines the Significant Events that authorize the USEC Board to approve a plant closing.

As a party to the Agreement, the Treasury Department has an interest in receiving information concerning proposed plant closings. Accordingly, we would like to review and comment on the legal justification for any proposed plant closing prior to any meeting of your Board of Directors which may consider such a closing.

If USEC is considering a closing based upon the occurrence of one or more Significant Events, please notify the Treasury Department immediately and provide the factual basis for concluding that a Significant Event has occurred or is likely to occur in the near future. It is important that the Treasury Department has ample time to evaluate independently the merits of such a plan, so that it may verify USEC's adherence to the requirements of the Agreement.

Thank you for your assistance on this matter.

Sincerely,

Gary Gensler
Under Secretary for Domestic Finance

Ratings on USEC Inc. Lowered; Outlook Negative

Scott Sprinzen, New York (1) 212-438-7812

NEW YORK (Standard & Poor's CreditWire) Feb. 4, 2000--Standard & Poor's today lowered its ratings on USEC Inc. (see list below).

The current outlook is negative.

The downgrade reflects greater-than-anticipated intensification of competition. USEC's financial performance is being hurt by continuing erosion in the price of its main product, enriched uranium. Pricing pressure is resulting from excess production capacity industrywide, exacerbated by aggressive efforts by competitors to gain market share, the liquidation of safety stocks that had been held by certain customers and countries, and exports to the U.S. market by Kazakhstan, which has been able to circumvent trade barriers. Standard & Poor's does not anticipate any near-term improvement in prices.

Adding to the challenges for USEC is its role as marketer of material for AO Techsnabexport ('Tenex'; unrated), a Russian government entity. Under its contract with Tenex, USEC is obligated to purchase enriched uranium from Tenex at a price that now exceeds its own unit production cost. With the decline in market prices, this arrangement has become increasingly burdensome for USEC. To date, efforts by USEC to renegotiate pricing under the contract and to obtain relief from the U.S. government have been unsuccessful. While USEC might ultimately choose to withdraw from the arrangement with Tenex, the company would thereby run the risk that the Russian material would destabilize the world market for enriched uranium -- as occurred in the early 1990s.

USEC has also been adversely affected by rising costs. Material purchased from Tenex has displaced USEC's own production, causing unit production costs to rise. USEC has also been affected by rising electric power costs -- this being the largest component of its cost structure and by unfavorable currency exchange rate movements. Management has initiated aggressive cost-cutting actions, such as the just-announced plan to reduce its work force by 850 employees, but these are unlikely to fully offset adverse market conditions and cost pressures. USEC had been expected to replace its current production technology with a new laser-based technology, which it was hoped would significantly improve the company's cost position, but development efforts were terminated during 1999 due to poor economics. USEC is now in the process of evaluating alternative technologies.

USEC's earnings prospects have deteriorated considerably. Management has stated that net income for the fiscal year ended June 30, 2000, is expected to total a weak $110 million

to $115 million (before restructuring charges), and decline to between $35 million and $45 million during fiscal 2001. In contrast, USEC's internal cash flow generation remains relatively strong, but this largely reflects the planned liquidation of its natural uranium inventories, which will be depleted in 5 to 6 years. In reaction to the weakness of its common share price, USEC initiated share repurchases during 1999, and a new 20 million share repurchase program has just been announced (worth about $118 million at the current share price): implementation of this program would more than offset the cash savings resulting from the just-announced cut to its common dividend. Still, USEC's financial flexibility should remain adequate, in light of the company's moderate debt usage and the availability of borrowings under its bank credit facility.

OUTLOOK: NEGATIVE.

Ratings would be jeopardized by further erosion in pricing, or if management's cost cutting efforts fail to stabilize earnings, Standard & Poor's said. -- CreditWire

RATINGS LOWERED

	To	From
USEC Inc.		
Corporate credit rating	BB+	BBB
Short-term corporate credit rating	B	A-2
Senior unsecured debt	BB+	BBB
Bank loan rating	BB+	BBB
Commercial paper	B	A-2

Credit Profile:

see above

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Susan D. Abbott
Managing Director
Corporate Finance
Moody's Investors Service
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New York
Carol Cowan, VP-Senior Analyst
Mo-Ying Seto, SVP
Corporate Finance
Moody's Investors Service
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SUBSCRIBERS: (212) 553-1653

MOODY'S DOWNGRADES USEC INC'S SENIOR UNSECURED GUARANTEED BANK CREDIT FACILITY TO Baa3, SENIOR UNSECURED DEBENTURES TO Ba1 AND SHORT TERM DEBT RATING TO P-3

Approximately $800 Million of Debt Securities Affected

New York, February 23, 2000 -- Moody's Investors Service downgraded USEC Inc's senior unsecured guaranteed bank credit facility to Baa3, senior unsecured debentures to Ba1 and the short term debt rating to P-3. The rating action reflects Moody's concerns over USEC's ongoing earnings and cash flow contraction and the resultant degradation in debt protection measurements. This situation is attributable to persistent depressed market conditions for enriched uranium and USEC's increasing production costs on significantly reduced output levels at its plants.

The following ratings are affected:

USEC Inc - senior unsecured, guaranteed bank credit facility to Baa3 from Baa1, senior unsecured debentures to Ba1 from Baa1, short term debt rating to P-3 from P-2

The outlook is negative. Ratings will continue under pressure due to the continued high cost base relative to SWU prices and the expectation that prices are unlikely to improve from current levels of approximately $80/SWU given overcapacity in the market. While recently announced initiatives concerning employment levels and power costs will provide savings, Moody's expects earnings compression to continue on the present operating profile and market conditions Additionally, the use of excess cash flow generated to buy back stock will weaken USEC's liquidity position.

As a global leader in providing uranium enrichment services, USEC continues to demonstrate a solid market share (approximately 75% of domestic market and 40% of global market) Although the company's backlog is in excess of $6 billion, portfolio realizations will continue to contract over time as lower price contracts replace higher price contract run offs USEC's deteriorating financial performance stems from a number of factors, some of which remain outside the company's control. Overcapacity in the market and depressed SWU prices, which appear stuck at approximately $80 will, over time, impact revenues to an increasing degree The purchase of enriched uranium under the Russian contract, for which they act as the U S government's executive agent, is at a price in excess of current market prices While the company has advised that it is in discussions to negotiate a market based pricing mechanism, such would not become effective until January 2002 Going forward, annual volumes purchased under the Russian contract (5 5 million SWU) will cause USEC to cut back production at its own plants to a level around 25% of nameplate capacity, thereby significantly increasing

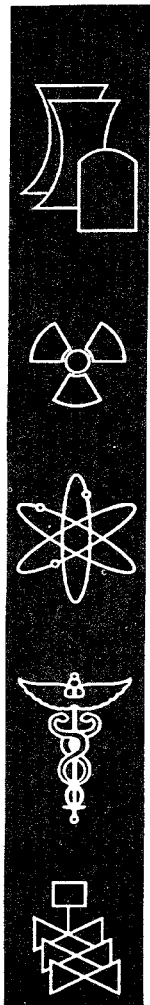
production costs on a per unit basis. Power costs have risen dramatically as well and the company is in discussions to achieve supply agreements for the summer months similar to those negotiated in calendar 1999. On its present operational basis and with the initiatives that the company has announced, USEC indicates that net income for fiscal 2001 will be in the range of $35 -$45 million versus the indicated forecast of $110 million for fiscal 2000. Going forward, interest coverage and other debt protection ratios may contract to a level not commensurate with an investment grade rating. USEC continues to demonstrate adequate cash generating capability over the near term, indicating an average over the 2000 and 2001 period of $188 million per year prior to dividends, share repurchase and debt repayment. The level of cash flow generated will, however, remain sensitive to the level of uranium sold from the stockpile transferred by the Department of Energy under the Privatization Act. The share buy back program and continued earnings contraction will also pressure cash flow.

Certain payment timing differences and USEC's share repurchase program during the first half of its fiscal 2000 contributed to a more leveraged position of 40% compared to 33% at June 30, 1999. Implementation of the additional share repurchase program, for up to 20 million shares by June 2001, will be a limiting factor in improvement in the leverage ratio notwithstanding the reduction in the dividend payout.

USEC Inc., headquartered in Bethesda, Maryland, had sales of $1.5 billion in its fiscal year ended June 30, 1999.

end

NUREG-1671



Standard Review Plan for the Recertification of the Gaseous Diffusion Plants

Draft Report for Comment

U.S. Nuclear Regulatory Commission
Office of Nuclear Material Safety and Safeguards
Washington, DC 20555-0001

USEC

16.0 DETERMINATION OF FOREIGN OWNERSHIP, CONTROL, OR DOMINATION, COMMON DEFENSE AND SECURITY, AND RELIABLE AND ECONOMICAL SOURCE OF DOMESTIC ENRICHMENT SERVICES

16.1 Responsibility for Review

16.1.1 Primary: As designated

16.1.2 Secondary: Facilities Security Specialist/Safeguards Technical Analyst

16.1.3 Supporting: Material Control and Accounting Inspector/Resident Inspector

16.2 Purpose of Review

The purpose of this review is to determine that an applicant for certification is not owned, controlled, or dominated by an alien, a foreign corporation, or a foreign government; that issuance of a certificate would not be inimical to the common defense and security of the United States; and that issuance of a certificate would not be inimical to the maintenance of a reliable and economical domestic source of enrichment services.[1]

16.3 Areas of Review

General

An application to transfer certificates will be reviewed to examine the changes proposed in the application for the transfer from that which is currently approved or permitted under the existing certificates.

Foreign Ownership, Control, or Domination

Information submitted by the applicant, as specified in "Foreign Ownership, Control, or Influence Guidance Documents for the Privatization of the United States Enrichment Corporation," will be reviewed. This information includes, but is not limited to:

1. Portions of securities held by foreign entities or held by means that prevent the identification of the beneficial owner

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[1] Note: the procedures in this SRP for a statutory determination of foreign ownership, control, or domination, are not to be used to determine foreign ownership, control, or influence (FOCI) for granting access to classified material. The NISPOM is the governing document for determining FOCI and the granting of access to classified material.

Determination of Foreign Ownership

2. Management positions held by non-U.S. citizens

3. Ability of foreign entities to control the appointment of management positions

4. Contracts and other agreements with foreign entities

5. Finance and revenue sources involving foreign entities

Common Defense and Security

The following items will be reviewed for compliance with NRC regulatory requirements to protect the common defense and security:

1. Physical Security Plan

2. Security Plan for the Protection of Classified Matter

3. Fundamental Nuclear Material Control Plan

4. Inspection, event, and resident inspector reports dealing with facility and transportation physical protection, material control and accounting, information security programs, and control of classified material

5. Information regarding the impact of the Russian HEU Agreement, and any related contracts, on the financial viability of the applicant

6 An assessment of the performance of the applicant as the executive agent of the U.S. for the Russian HEU Agreement in consultation with members of the HEU Oversight Committee

Reliable and Economical Source of Domestic Enrichment Services

Assessments of the financial viability of the applicant will be reviewed. The assessments will be based on the actual or estimated credit rating of the applicant, a standard used by the financial community to objectively measure an entity's financial condition, and its ability to meet its obligations, and other economic, financial and business characteristics. The current public credit rating of the applicant, published by a recognized credit rating agency (e.g., Standard & Poor's, Moody's Investor Service, Duff & Phelps, or Fitch), will be reviewed. If (I) the applicant does not have a current public credit rating, or (ii) in the case of a transfer of the certificates, a public credit rating would not apply to the applicant after the transfer, then an assessment of the financial viability of the applicant, based upon an estimate of the applicant's credit rating, will be reviewed. This estimated credit rating will be based on quantitative and qualitative analyses of the financial and business risks of the applicant.

16.4 Review Procedures

The reviewer should determine whether the applicant is subject to any of the criteria set forth in 10 CFR Part 76.22, "Ineligibility of Certain Applicants."

16.4.1 Foreign Ownership, Control, or Domination

An applicant is considered to be foreign owned, controlled, or dominated whenever a foreign interest has the power, direct or indirect, whether or not exercised, and whether or not exercisable, through the ownership of the applicant's securities, by contractual arrangements, or other means, to direct or decide matters affecting the management or operations of the applicant.

A foreign interest is defined as any foreign government, agency of a foreign government, or representative of a foreign government; any form of business enterprise or legal entity organized, chartered or incorporated under the laws of any country other than the U.S. or its possessions and trust territories; any person who is not a citizen or national of the U.S; and any U.S. interest effectively controlled by one of the above foreign entities.

The reviewer should assess the following items to determine if the applicant is foreign owned, controlled, or dominated:

1. The applicant should provide answers to the following questions. If any of the answers are affirmative, the applicant should furnish detailed information that describes all conditions that exist. The information will be considered in the aggregate and the fact that some of the below listed conditions may apply does not necessarily render the applicant company ineligible for certification.

   a. Does a foreign interest own or have beneficial ownership in 5% or more of your organization's voting securities?

   b. Does your organization own 10% or more of any foreign interest?

   c. Do any foreign interests have management positions such as directors, officers, or executive personnel in your organization?

   d. Does any foreign interest control or influence, or is any foreign interest in a position to control or influence the election, appointment, or tenure of any of your directors, officers, or executive personnel?

   e. Does your organization have any contracts, binding agreements, understandings, or arrangements with a foreign interest(s) that cumulatively represent 10% or more of your organization's gross income?

   f. Is your organization indebted to foreign interests?

   g. During your last fiscal year, did your organization derive 5 percent or more of its total revenues or net income from any single foreign interest or in the aggregate 30 percent or

more of its revenues or net income from foreign interests?

h. Is 5% or more of any class of your organization's securities held in "nominee shares", in "street names", or in some other method which does not disclose beneficial owner of equitable title?

I. Does your organization have interlocking directors/officers with foreign interests?

j. Are there any citizens of foreign countries employed by, or who may visit, your offices or facilities in a capacity which may permit them to have access to classified information or a significant quantity of special nuclear material?

k. Does your organization have foreign involvement not otherwise covered in your answers to the above questions?

2. The reviewer should obtain a foreign intelligence threat assessment. This assessment will be conducted through the Intelligence Community and others, and will be coordinated by the Department of Energy. The reviewer may obtain the assessment by contacting the DOE representative to the HEU Oversight Committee.

3. If the applicant submits any affirmative information listed in section 16.5.1, steps 1.a through 1.k above, or the foreign intelligence threat assessment contains information, that the applicant may be foreign owned, controlled, or dominated, the reviewer shall determine:

   a. the nature and extent of foreign ownership, control, or domination, to include whether a foreign interest occupies a controlling or dominant minority position;

   b. the source of foreign ownership, control, or domination, to include identification of immediate, intermediate, and ultimate parent organizations; and

   c. the type of actions, if any, that would be necessary to negate the effects of foreign ownership, control, or domination to an acceptable level.

4. If it is determined that an applicant company may be considered to be foreign owned, controlled, or dominated, or that additional action would be necessary to negate the foreign ownership, control, or domination, the applicant shall be promptly advised and requested to submit a negation action plan. In cases that involve foreign ownership, a plan may consist of one of the methods described in Chapter 2, Section 2-306, of the NISPOM. When factors not related to ownership are present, the plan shall provide positive measures that assure that the foreign interest can be effectively denied control or domination. Examples of such measures include: modification or termination of loan agreements, contracts and other understandings with foreign interests; diversification or reduction of foreign source income; demonstration of financial viability independent of foreign interests; elimination or resolution of problem debt; assignment of specific oversight duties and responsibilities to board members; adoption of special board resolutions; and other actions that negate foreign control or domination.

5. The reviewer shall arrange to meet with, or otherwise communicate these findings to, the principal members of the HEU Oversight Committee and obtain their comments.

6. The reviewer shall ensure that NRC remains informed regarding foreign ownership, control, or domination by preparing certificate conditions of the following types:

   If, at any time after the privatization date, the Corporation obtains information reasonably indicating changes described in the National Industrial Security Program Operating Manual, DOD 5520.22-M, January 1995 (NISPOM), Chapter 1, Section 3, 1-302(h), to the information previously submitted to NRC, described in the NISPOM, Chapter 2, Section 3, 2-302 b. (1) through (11), the Corporation shall notify NRC in writing within 15 days.

   If the Corporation enters into negotiations for the proposed merger, acquisition, or takeover by a foreign person, the Corporation shall submit notification to NRC, in writing, within 15 days of the commencement of such negotiations. The submission shall include the type of transaction under negotiation (stock purchase, asset purchase, etc.), the identity of the potential foreign person investor, a plan to negate foreign ownership, control, or domination, and copies of any related loan, purchase and shareholder agreements, annual reports, bylaws, articles of incorporation, partnership agreements, and reports filed with other federal agencies.

16.4.2 Common Defense and Security

1. The reviewer should determine that the applicant's Physical Security Plan and Fundamental Nuclear Material Control Plan have been reviewed and approved by the appropriate NMSS personnel.

2. The reviewer should consult with the Division of Facilities and Security to determine that the applicant's Security Plan for the Protection of Classified Matter has been reviewed and approved.

3. If the applicant has previously been issued a certificate of compliance, the reviewer should ensure that NRC inspection reports and resident inspector reports do not indicate a general failure to protect the common defense and security interests of the United States.

4. The reviewer should consider the impact of executing contracts associated with the Russian HEU agreement on the financial viability of the applicant. The analysis of the applicant's financial viability, described below, should include information concerning the cost of procuring Russian material, the amount of material the applicant has contracted to procure, the costs of enrichment services provided by the applicant, and current market prices. This information should allow the reviewer to gauge whether executing such contracts might be a significant economic disadvantage, or favorable to an extent that would motivate the applicant to reduce the production of domestic enrichment services.

5. The reviewer should arrange to meet with, or otherwise consult with, the principal members of the HEU Oversight Committee to obtain the committee's assessment of the applicant's

performance as the U.S. Agent for the Russian HEU Agreement.

6. The reviewer shall ensure that NRC remains informed regarding the applicant's performance as the U.S. agent for the Russian HEU Agreement by preparing a certificate condition of the following type:

   USEC, or its successors, as the Executive Agent for the United States for implementing the Russian HEU Agreement, shall notify NRC in writing within 15 days, if at any time and for any reason, including actions of third parties, USEC or its successors become aware of, or anticipate, any change in the provisions of, or in the implementation of, the terms of the "Memorandum of Agreement Between the United States Acting By and Through the United States Department of State, and the United States Department of Energy and the United States Enrichment Corporation, for USEC to Serve as the United States Government's Executive Agent Under the Agreement Between the United States and the Russian Federation Concerning the Disposition of Highly Enriched Uranium Extracted from Nuclear Weapons," entered into as of April 18, 1997.

16.4.3 Reliable and Economical Source of Domestic Enrichment Services

Issuance of a certificate of compliance should be considered inimical to the maintenance of a reliable and economical source of domestic enrichment services if the applicant does not have a sufficiently strong financial condition to allow the expectation that it can remain viable for at least five years.

The review should consist of the following procedures. (If the staff elects to have a contractor conduct these procedures, the staff should review the contractor's analysis and findings and either concur with the findings or specify the staff's basis for taking a different position.)

1. If the applicant has one or more current credit ratings issued by a recognized rating agency (e.g., Standard & Poor's Corp., Moody's, Investors Service, Duff & Phelps Credit Rating Co., or Fitch Investors Services, L.P.), the reviewer should determine whether the lowest such rating is of investment grade (e.g., AAA, AA, A, or BBB as rated by Standard & Poor's, or Aaa, Aa, A, or Baa as rated by Moody's) or below investment grade (e.g., BB, B, CCC or lower as rated by Standard & Poor's, or Ba, B, Caa or lower as rated by Moody's).

2. If the applicant does not have a current credit rating issued by a recognized rating agency, the reviewer should conduct an independent analysis to estimate a credit rating and determine whether the estimated credit rating is of investment grade. The estimated credit rating should be based on quantitative and qualitative analysis of information provided by the applicant, including information regarding the applicant's parent company or companies, to the extent that they might affect the financial condition of the applicant.

   a. The reviewer should ensure that NRC has received the following information from the applicant:

(1) The types, amounts, and holders of debt and the types and amounts of equity of the applicant. In the case of the privatization of USEC, the method of financing to be used to purchase USEC (if applicable); and the types, amounts, and holders of any debt and the types and amounts of equity of the privatized entity;

(2) A five-year business plan addressing the applicant's enrichment business line as well as other anticipated business lines, including alternative enrichment technologies such as AVLIS, that will require investments of capital (including working capital) by the applicant, and the portion of projected revenue, for each of the five years, covered by contracts in existence at the time of the application;

(3) All significant business and economic assumptions underlying the plan;

(4) Pro forma financial statements for the applicant for each of the next five years;

(5) Current financial statements (if applicable) for the applicant, and in the case of privatization, for USEC, along with an independent certified public accountant's opinion on the financial statements;

(6) Identification of the applicant's proposed directors and officers and a discussion of their qualifications to provide financial and business management;

(7) The organizational structure of the applicant and its relationship to corporate parents and other affiliates; and

(8) Information on the financial condition of the applicant's corporate parents, including credit ratings, profiles prepared by the investment industry, and/or audited financial statements reflecting the three most recently completed fiscal years.

b. The reviewer should ensure the items specified above are consistent, and that they provide a comprehensive and reasonable picture of the applicant. If pro forma financial statements are based on inconsistent or unrealistic assumptions, it may be necessary to discuss with the applicant the basis of the projections.

c. The reviewer should quantitatively assess the financial characteristics of the applicant relative to available historical benchmarks. Some corporate financial analysis expertise will be necessary to complete this step. The reviewer may wish to obtain one or more financial texts for reference, such as Standard & Poor's "Corporate Ratings Criteria." The reviewer's analysis should include the following measures:

(1) Size Measures

- Net sales
- Net income
- Total assets
- Net worth

(2) Capital Structure Ratios

- Total debt ÷ capitalization
- Total debt ÷ equity
- Long-term debt ÷ capitalization

(3) Coverage Ratios

- Net income plus depreciation and other noncash items ÷ total debt
- Pretax income plus interest expense ÷ gross interest
- Pretax income plus depreciation and other noncash items plus interest expense ÷ gross interest

(4) Profitability Ratios

- Net income ÷ total assets
- Pretax income plus interest ÷ total assets
- Net income ÷ equity
- Operating income ÷ sales

Other ratios and measures, addressing the above categories or other financial characteristics may be used if they provide a measure of the applicant's financial condition (e g., see "Corporate Ratings Criteria").

d. The reviewer should also consider qualitative factors in light of the financial analysis. Factors to be assessed include the applicant's competitive position, market environment, quality of management, and financial and business risks. These factors should be considered in proportion to their potential impacts on the applicant.

e. The reviewer should evaluate the financial condition of the applicant's corporate parents and affiliates to the extent that they might affect the applicant's financial condition. The financial condition of corporate parents or affiliates should be should be considered in proportion to the potential impact on the applicant.

f. Based on the preceding steps, the reviewer should establish an estimated credit rating of the applicant. In establishing the estimated rating, the reviewer should first determine what the estimated rating would be if it were based solely on an analysis of the applicant's financial ratios and size measures relative to available benchmarks. The reviewer should then adjust the estimated credit rating based on other considerations identified above. Adjustments should be proportional to each factor's potential impacts on the applicant. Assignment of a specific estimated rating (e.g., AA versus A) is not necessary if the reviewer is able to determine that the estimated credit rating is investment grade. Assignment of a specific rating may be necessary if the estimated rating is below investment grade.

3. If the actual or estimated credit rating is of investment grade, the reviewer should find that

the applicant has sufficiently strong financial condition to allow it to remain viable for at least five years, and that issuance of a certificate of compliance would not be inimical to the maintenance of a reliable and economical source of domestic enrichment services. If the actual or estimated credit rating is below investment grade, the reviewer should consider whether any other economic, financial, or business characteristics (e.g., contracts adequate to support the applicant's operations over a five-year time period, financial guarantees provided by a parent company, compelling business prospects) exist that provide reasonable assurance of the applicant's viability for at least five years. If the reviewer finds that such factors exist, and that the applicant is expected to remain viable for at least five years, then the reviewer should find that issuance of a certificate of compliance would not be inimical to the maintenance of a reliable and economical source of domestic enrichment services. However, if the reviewer finds that such factors do not exist, then the reviewer should find that issuance of a certificate of compliance to the applicant may be inimical to the maintenance of a reliable and economical source of domestic enrichment services.

16.5 Acceptance Criteria

16.5.1 Regulatory Requirements

10 CFR § 76.22 addresses the ineligibility of applicants for certification if the Commission determines that:

1. The Corporation is owned, controlled, or dominated by an alien, a foreign corporation, or a foreign government; or

2. The issuance of such a certificate of compliance would be inimical to:

   a. The common defense and security of the United States; or

   b. The maintenance of a reliable and economical domestic source of enrichment services.

10 CFR § 76.33 provides for NRC to require the applicant to supply additional information as necessary.

10 CFR § 95.15 addresses the collection of information necessary to determine that the applicant is not owned, controlled, or dominated by an alien, foreign corporation, or foreign government.

10 CFR Parts 76 and 95 contain and reference applicable regulatory requirements necessary to protect the common defense and security.

16.5.2 Regulatory Guidance

Regulatory guidance applicable to the areas of review in this chapter are:

1. U.S. Nuclear Regulatory Commission, NUREG/CR-5734, "Recommendations to the NRC on

Acceptable Standard Format and Content for the Fundamental Nuclear Material Control (FNMC) Plan Required for Low-Enriched Uranium Enrichment Facilities," Nov. 1991

2. U.S. Nuclear Regulatory Commission, Reg Guide 5.67, "Material Control and Accounting for Uranium Enrichment Facilities Authorized to Produce Special Nuclear Material of Low Strategic Significance," Dec. 1993

3. U.S. Nuclear Regulatory Commission, "Security Plan Format and Content Guide for NRC Licensees, Certificate Holders, and Related Organizations," March 1994

16.5.3 Regulatory Review Criteria

The application is acceptable if the following criteria are met:

Foreign Ownership, Control, or Domination

After a review of the potential foreign involvement information in accordance with the Review Procedures, section 16.5.1, the reviewer determines that no foreign interest has the ability, direct or indirect, whether or not exercised, to direct or decide matters affecting the management or operations of the applicant.

The following additional criteria are applicable in the case of privatization of USEC:

1. Foreign competitors of USEC are precluded from participating in any acquisition of USEC.

2. Entities with a substantial commercial relationship with foreign enrichment providers, with respect to uranium and uranium products, are precluded from participating in any acquisition of USEC.

3. Foreign interests own no more than 10 percent of the outstanding voting securities of the applicant.

4. Foreign sourced financing of an acquisition of USEC is no more than 10 percent of the purchase price.

Common Defense and Security

1. The applicant's Physical Security Plan has been reviewed and approved.

2. The applicant's Security Plan for the Protection of Classified Matter has been reviewed and approved.

3. The applicant's Fundamental Nuclear Material Control Plan has been reviewed and approved.

4. If the applicant has previously been issued a certificate of compliance, a review of NRC

inspection reports and resident inspector reports does not indicate a general failure, by the applicant, to protect the common defense and security interests of the United States.

5. Consultation with the principal members of the HEU Oversight Committee indicates that the applicant's performance as the U.S. Agent for the Russian HEU Agreement is acceptable.

Reliable and Economical Source of Domestic Enrichment Services

1. The applicant's current actual or estimated public credit rating is investment grade (e.g. Standard & Poor's AAA to BBB, Moody's Aaa to Baa); or

2. The applicant's current actual or estimated public credit rating is not investment grade, but other economic, financial, or business characteristics exist that strongly indicate the entity's viability for at least five years.

16.6 Evaluation Findings

After evaluating the application and the supporting information, and determining the information to be adequate and the acceptance criteria to be met, the reviewer will prepare a statement, similar to the following, for inclusion in the Certificate Evaluation Reports:

On the basis of the staff's review and evaluation of the application for certification, the staff has found no cause to determine that:

1. the applicant is owned, controlled, or dominated by an alien, a foreign corporation, or a foreign government; or

2. issuance of a certificate of compliance would be inimical to the common defense and security of the United States; or

3. issuance of a certificate of compliance would be inimical to the maintenance of a reliable and economical domestic source of enrichment services.

16.7 References

U.S. Department of Defense, "National Industrial Security Program Operating Manual (NISPOM)," DOD 5520.22-M, Jan. 1995.

U.S. Department of Energy, U.S. Nuclear Regulatory Commission, U.S. Enrichment Corporation, "Foreign Ownership, Control, or Influence Guidance Documents for the Privatization of the United States Enrichment Corporation."

Read

IMPLEMENTING THE HEU AGREEMENT

Current Issues: The United States Enrichment Corporation (USEC) has experienced financial difficulties since it became a private corporation in July 1998. The total return on the stock is –27.9% over the last year. What, if any, are the implications of USEC's performance as executive agent for implementation of the 1993 U.S.-Russian HEU Purchase Agreement? Will USEC back out as executive agent in the near term? Can USEC sustain its role in the long term? What are the implications for U.S. planning, policy and actions?

Impact of HEU Agreement on USEC: USEC attributes many of its problems to the costs of its current role as U.S. executive agent in implementing the HEU Agreement (see appendix). Under that agreement, the U.S. has contracted to purchase the material derived from 500MT of HEU from Russian weapons over twenty years. USEC purchases separative work units (SWU) derived from Russian weapons and sells it to utilities for reactor fuel. This track of the deal is worth roughly $8B to Russia over the life of the agreement. For the balance of the HEU Agreement until 2013, Russia is scheduled to provide roughly 5.5 million SWU per year – nearly half of U.S. annual demand. From USEC's standpoint, the purchase of Russian SWU (currently $89.50/SWU) displaces SWU they produce more cheaply in the U.S.

USEC's Challenges and Impact on HEU Agreement: USEC, however, faces serious constraints other than the HEU Agreement. USEC, while remaining dominant in the U.S. market for enrichment services, faces a slightly declining market share in a more competitive market. USEC's average sales price is $115.40/SWU, a price that will fall as new contracts with lower prices start to dominate their sales. USEC has commitments to run two aging gaseous diffusion plants (GDPs), no proven enrichment technology for its production in the future, and a large dividend payment to stockholders. Sustaining the cash flow for the dividend cuts against near term investments needed to sustain, consolidate or improve enrichment operations. As a result, USEC has been selling natural uranium stocks received through privatization and conversion services to raise cash to sustain itself. Natural uranium prices have as a result fallen to new lows, despite the March 1999 U.S.-Russian Transfer Agreement to intended to shore up the natural uranium track of the HEU Agreement.

USEC's Appeal to the Government: Against this backdrop, USEC has urged the executive and legislative branches to take measures to assist its economic position in the interest of sustaining the HEU Agreement. USEC has also sought to get Russia to agree to lower the costs of the SWU it purchases from Russia in 2000, rather than 2002 when the current contract would open the issue (although the Russians apparently feel no compulsion to lower their returns to benefits USEC shareholders). If USEC does not receive relief, it could withdraw from its role as the U.S. agent for the HEU Agreement before the U.S. has had a chance to fully develop an alternative. In addition, USEC might choose to close the Portsmouth, Ohio plant in the near term, this would save the company approximately $113 million per year, but would cause unemployment for 1500 people that were provided some reassurance in a 1998 Treasury Agreement that they would be employed through 2004. Informally, USEC has suggested that they need $100 million per year for the next two years, 2000 and 2001, to avoid such outcomes.

Reviewing the Options: This paper explores a range of options that the U.S. might consider to address HEU Agreement implementation in the near term. They range from direct appropriations to doing nothing beyond preparing for the market to take its course; some could be pursued together. This paper does *not* address in detail how the U.S. might use these options in negotiations with USEC (e.g. restraints on natural uranium sales, worker benefits, limits on management benefits) or the Russians, the likelihood of USEC

USEC INC.

MANAGEMENT'S DISCUSSION AND ANALYSIS OF
FINANCIAL CONDITION AND RESULTS OF OPERATIONS

The following discussion should be read in conjunction with, and is qualified in its entirety by reference to, the consolidated financial statements and related notes and management's discussion and analysis of financial condition and results of operations included in the Annual Report on Form 10-K for the fiscal year ended June 30, 1999.

RESULTS OF OPERATIONS - THREE AND SIX MONTHS ENDED DECEMBER 31, 1999 AND 1998

Revenue

Revenue from the sale of SWU amounted to $431.8 million in the three months ended December 31, 1999, an increase of $18.0 million (or 4%) over the $413.8 million in the corresponding period of fiscal 1999. In the six months ended December 31, 1999, revenue was $637.0 million, a reduction of $84.5 million (or 12%) from the $721.5 million in the fiscal 1999 period.

Changes in revenue in the fiscal 2000 periods resulted from a reduction in average prices for separative work units ("SWU") billed to customers, changes in timing of customer nuclear reactor refueling orders, and lower SWU commitment levels of two domestic and a foreign customer. Average SWU prices billed to customers declined 9% and 5% in the three and six months ended December 31, 1999, respectively, compared with the fiscal 1999 periods.

The volume of SWU sold increased 14% in the three months ended December 31, 1999, but declined 7% in the six months ended December 31, 1999, compared with the corresponding periods of fiscal 1999. Revenue and operating results can fluctuate significantly from quarter-to-quarter, and in some cases, year-to-year. Customer requirements are determined by refueling schedules for nuclear reactors, which generally range from 12 to 18 months (or in some cases up to 24 months), and are in turn affected by, among other things, the seasonal nature of electricity demand, reactor maintenance, and reactors beginning or terminating operations.

Revenue in the three months ended December 31, 1999, includes sales of $42.8 million to customers in Japan to replace SWU stranded at the Tokai-mura uranium processing facility in Japan. Operations at the facility were suspended in September 1999 following an incident involving highly enriched uranium for an experimental reactor. Nuclear fuel services sold by USEC were not involved in the incident. Additional sales to Japanese customers affected by the incident

are expected during the remainder of fiscal 2000. As SWU is retrieved from the facility and used by the Japanese customers in fiscal years 2001 and 2002, USEC's sales to such customers may be reduced.

USEC's financial performance over time can be significantly affected by changes in the market price for SWU. As older customer contracts with higher prices expire, USEC's backlog is becoming more heavily weighted with newer contracts with shorter terms and lower prices. In light of this, USEC expects that its backlog will decline over time unless new SWU commitments are added at sufficient levels to offset the impact of shorter term contracts, expiring commitments and lower prices.

Revenue from sales of uranium, primarily uranium hexafluoride, amounted to $15.8 million and $41.5 million in the three and six months ended December 31, 1999, compared with $8.6 million and $8.8

million in the corresponding periods in fiscal 1999. The level of uranium sales is consistent with USEC's long-range plans developed at the time of privatization. Although uranium prices have declined in the six months ended December 31, 1999, compared with the corresponding period in fiscal 1999, sales of uranium from inventory are expected to continue to generate cash flow.

The percentage of revenue from domestic and international customers follows:

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	THREE MONTHS ENDED DECEMBER 31,		SIX MONTHS ENDED DECEMBER 31,	
	1999	1998	1999	1998
<S>	<C>	<C>	<C>	<C>
Domestic	62%	54%	56%	56%
Asia	35	41	39	34
Europe and other	3	5	5	10
	100%	100%	100%	100%

</TABLE>

Revenue from domestic customers declined $29.3 million (or 7%), revenue from customers in Asia increased $16.4 million (or 7%), and revenue from customers in Europe and other areas declined $38.9 million (or 54%) in the six months ended December 31, 1999, compared with the corresponding period of fiscal 1999. The changes in the geographic mix of revenue resulted primarily from replacement SWU sales to Japan, the timing of customers' orders, and the growth in sales of uranium.

Cost of Sales

Cost of sales is based on the quantity of SWU sold during the period and is dependent upon production costs at the plants and purchase costs primarily under the Russian contract. Production costs consist principally of electric power, labor and benefits, depleted uranium disposition costs, materials, and maintenance and repairs. Under the monthly moving average inventory cost method, an increase or decrease in production or purchase costs will have an effect on cost of sales over current and future periods.

Cost of sales amounted to $377.4 million in the three months ended December 31, 1999, an increase of $46.7 million (or 14%) compared with $330.7 million in the corresponding period in fiscal 1999. Cost of sales in the six months ended December 31, 1999, was $563.8 million, a decline of $15.5 million (or 3%) from the $579.3 million in the corresponding period of fiscal 1999. The increase in cost of sales for the three months ended December 31, 1999, reflects the 14% increase in the volume of SWU sold and higher sales of uranium. Cost of sales continues to be adversely affected by increased purchases of SWU under the Russian contract and lower production at the plants. As a percentage of revenue, cost of sales amounted to 83% in the first six months of fiscal 2000, compared with 79% in the corresponding period of fiscal 1999.

USEC purchases a significant portion of its electric power based on long-term contracts with dedicated power generating facilities. Firm power costs vary depending on operating and capital costs incurred at the power generating facilities. Non-firm power costs vary seasonally with rates being higher during winter and summer as a function of the extremity of the weather. USEC's power costs are typically higher in the summer months as almost all of the power supplied to the Paducah plant in the summer months is purchased at market-based rates because it is non-firm power. In the summers of 1999 and 1998, production at the Paducah plant was reduced to mitigate the high cost of non-firm power.

Electric power costs amounted to $177.4 million in the first six months of fiscal 2000 (representing

52% of production costs) compared with $199.0 million (representing 55% of production costs) in the corresponding period of fiscal 1999, a reduction of $21.6 million (or 11%). Power supplied to and purchased for the Portsmouth plant in the six months ended December 31, 1999, was lower than in the corresponding period in fiscal 1999. USEC negotiated and implemented changes to its power supply agreements to limit exposure to high-cost, non-firm power prices at the Paducah plant, to monetize excess power available in the summer of 1999 under the contract to the Portsmouth plant, and to have the ability to move blocks of power in the summer of 1999 from the Portsmouth plant to the Paducah plant. USEC and one of its major suppliers are in negotiations for a similar supply agreement modification to be in place for the summer of the year 2000. In the six months ended December 31, 1998, persistent hot weather, high electricity demand in the Midwest and power generation shortages had contributed to record high power costs at the Paducah plant.

Costs for labor included in production costs declined 7% compared with the first six months of fiscal 1999. The average number of employees at the plants declined 9% in the first six months of fiscal 2000 compared with the corresponding period in fiscal 1999. In fiscal 1998, USEC had recorded a special charge of $12.8 million for costs related to severance benefits to be paid to plant workers in connection with workforce reductions, of which $11.8 million had been paid with respect to 470 workers as of December 31, 1999.

During fiscal 1999 and most of the six months ended December 31, 1999, SWU unit production costs at the Portsmouth plant were adversely affected by low production facility capability due to sub-optimal gaseous diffusion production equipment availability. A significant improvement in equipment availability was achieved in the three months ended December 31, 1999.

Pursuant to the agreement with the U.S. Treasury, USEC has committed to

continue operation of the two plants until at least January 2005, subject to limited exceptions, including:

- events beyond the reasonable control of USEC, such as natural disasters;
- a decrease in annual worldwide demand to less than 28 million SWU;
- a decline in the average price for all SWU under USEC's long-term firm contracts to less than $80 per SWU (in 1998 dollars);
- a decline in the operating margin to below 10% in a consecutive twelve-month period;
- a decline in the interest coverage ratio to below 2.5x in a consecutive twelve-month period; or
- if the long-term corporate credit rating of USEC is, or is reasonably expected in the next twelve months to be, downgraded below an investment grade rating.

On February 4, 2000, Standard & Poor's revised its credit rating of USEC's long-term debt to below investment grade.

USEC is the Executive Agent of the U.S. Government under a government-to-government agreement to purchase the SWU component of enriched uranium recovered from dismantled nuclear weapons from the former Soviet Union for use in commercial electricity production. Cost of sales has been, and will continue to be, adversely affected by amounts paid to purchase SWU under the Russian contract. In addition, since the volume of Russian SWU purchases has increased, USEC has operated the plants at significantly lower production levels resulting in higher unit production costs. Global market prices for SWU have declined below the price being paid for SWU under the Russian contract. Based on preliminary discussions with the U.S. and Russian governments, USEC expects that prices for SWU purchased under the Russian contract will be aligned with market prices beginning in calendar year 2002.

SWU purchased from the Russian Federation represented 45% of the combined produced and purchased supply mix in the six months ended December 31, 1999, compared with 35% in the corresponding period in fiscal 1999. USEC has ordered 5.5 million SWU for delivery under the Russian

contract in calendar year 2000 and expects to order and purchase 5.5 million SWU in calendar 2001.

Gross Profit

Gross profit amounted to $114.7 million in the first six months of fiscal 2000, a reduction of $36.3 million (or 24%) from $151.0 million in the corresponding period in fiscal 1999. Gross margin was 17% compared with 21% in the first six months of fiscal 1999. The reduction reflects the 5% decline in average SWU prices billed to customers.

Project Development Costs

Project development costs amounted to $4.0 million in the first six months of fiscal 2000 compared with $58.8 million in the corresponding period in fiscal

SECURITIES EXCHANGE ACT OF 1934

Commission file number 1-14287
USEC INC.
(Exact name of registrant as specified in its charter)

DELAWARE	52-2107911
(State or other jurisdiction of incorporation or organization)	(I.R.S. Employer Identification No.)

2 DEMOCRACY CENTER, 6903 ROCKLEDGE DRIVE, BETHESDA MD	20817
(Address of principal executive offices)	(Zip Code)

Registrant's telephone number, including area code: (301) 564-3200

Indicate by check mark whether the registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days. Yes X No
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As of January 31, 2000, there were 90,541,000 shares of Common Stock, par value $.10 per share, issued and outstanding.

USEC INC.

QUARTERLY REPORT ON FORM 10-Q
FOR THE QUARTER ENDED DECEMBER 31, 1999

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PART I

Mr. BURR. The Chair would recognize himself at this time for the purposes of questions of Mr. Timbers.

Mr. Timbers, you said that there was a great effort to control costs and that all things are on the table. Tell me, was Mr. Strickland's remarks relative to your compensation accurate?

Mr. TIMBERS. Mr. Chairman, which part of Mr. Strickland's——

Mr. BURR. Let me rephrase the question. If you added up all the salary, the bonus, the stock options or dividends, whatever is in your package, what do you make on an annual basis?

Mr. TIMBERS. I make a salary of $600,000 a year, and the rest of compensation is at risk. Last year, there was a bonus approximately of 600,000; and the balance was in stock.

Mr. BURR. That stock would have been valued at what?

Mr. TIMBERS. I would have to check what the value was at that time. I am not sure right now.

Mr. BURR. Were those stock options you were referring to?

Mr. TIMBERS. Combination of stock options. Most of it was in stock options, and there was restricted stock as well.

Mr. BURR. When can you exercise those options?

Mr. TIMBERS. There is a vesting period that is—I think it is prorated over a 5-year period so one-fifth is vested in the first year, and then the second fifth is vested in the second year and so on through 5 years.

Mr. BURR. Let me ask you, we are in the 21st or 22nd month of the privatization. Was your salary bigger this year than last or less this year than the prior year?

Mr. TIMBERS. According to the agreements with the Treasury at the time of privatization, my compensation could not change for 6 months following privatization. After that 6-month period—we privatized in July 1998. That 6-months period expired in February 1999.

Mr. BURR. Where is your salary in compensation today relative to where it was for the first 6 months when it couldn't be changed?

Mr. TIMBERS. The first 6 months I think as Mr. Strickland indicated I think was $325,000.

Mr. BURR. It has gone up significantly.

Mr. TIMBERS. It has gone up from the government sector salary to a private sector salary.

Mr. BURR. Is your salary on the table as it relates to all things on the table?

Mr. TIMBERS. My salary has not been discussed in that context.

Mr. BURR. Let me ask you if you were fired today, how much would you walk away with with the agreements—I think he referred to a parachute.

Mr. TIMBERS. I would have to go back and check that. I can't quote you those numbers.

Mr. BURR. Can anybody behind you help you? Is it 3 years of pay? Am I close?

Mr. TIMBERS. I think it is approximately 3 years of pay.

Mr. BURR. So if you were fired, you would get 3 years of pay. If you quit, how much would you get?

Mr. TIMBERS. Zero.

Mr. BURR. Is that to the best of your knowledge? Do you need any help from the people behind you?

Mr. TIMBERS. If I were to quit, it would be zero. There is not compensation. I would point out, Mr. Chairman, that this compensation structure was evaluated by an outside independent company. It is structured so as to be comparable to like, similar size companies in similar type businesses.

Mr. BURR. Mr. Timbers, I am sure whoever did those calculations probably used something as a guide. I am not asking technical questions about USEC because I think that we have some people who are integrally interested, Mr. Strickland, Mr. Whitfield, but I did come out of business and I know that when a company's stock devaluates 75 percent, there is a board of directors that usually looks at the officer's salary first and tries to make adjustments that are reflective of that. The simple question I am asking you as president, as head of the board, has your board of directors come to you and said we need to talk to you about your salaries or have you talked to officers about the level of salaries?

Mr. TIMBERS. No, that discussion has not occurred.

Mr. BURR. So your salary and officers' salary is off the table when we talk about cost-cutting procedures as it relates to a company whose stock has depreciated 75 percent of its open value.

Mr. TIMBERS. Mr. Chairman, I said that discussion has not occurred.

Mr. BURR. Will it occur?

Mr. TIMBERS. There are not plans of that right now.

Mr. BURR. Did the changes in the market condition come as a surprise to you?

Mr. TIMBERS. There were expectations that it was a challenging environment in terms of the market. I think those expectations were reflected in our disclosure statement, both in the offering memorandum and subsequent 10-K and 10-Q statements.

Mr. BURR. If you had to close the facility today, which one would it be of the two?

Mr. TIMBERS. We don't have—we have not made any kind of determination of that sort.

Mr. BURR. Do you have any detailed plan on cost-cutting procedures?

Mr. TIMBERS. Pardon?

Mr. BURR. Do you have any detailed plan on cost-cutting procedures?

Mr. TIMBERS. Mr. Chairman, I still didn't——

Mr. BURR. Do you have any written plan on cost-cutting procedures?

Mr. TIMBERS. We are looking at a number of different alternatives of how we may be able to save costs for the company in terms of power, in terms of labor, in terms of plant operations and a variety of different scenarios have been looked at. Do they constitute a plan? We do have an operating plan in place that has a number of different scenarios being considered.

Mr. BURR. Your company recently purchased 10 million shares of its own stock back for an average price of $10 a share. You have already lost $55 million based upon my calculation of where the stock price is today at roughly $4.50. Explain how this has been an effective cost-cutting effort.

Mr. TIMBERS. The stock buy-back program that you refer to was initiated in July 1999; and at that time, there was a view in terms of purchasing that stock that it was an effective use of the cash of the corporation. Cash of the corporation belongs to the shareholder, and we need to make a determination as stewards of that cash for the shareholder as to how best to effectively deploy that cash. If a determination was made that the stock of the company was under valued at that time and that would be a good investment to make, that amount was I think completed at approximately the price you are talking about.

Mr. BURR. The Chair has really concluded the question it wanted to ask but would take this opportunity to make a statement that in fact the price of stock in the marketplace is indicative of what individual investors are willing to pay, based upon their comfort level of not only the business that the company is in but in the leadership of the individuals that run the company; and I think that, Mr. Timbers, for the trend that you suggest today, my No. 1 suggestion would be you need a written plan. Without a written plan, it puts everything on the table, everything, including salaries that don't reflect the trend that is currently happening to your company stock. I think with some certainty I would know what the value would be a year from now.

At this time the Chair would recognize Mr. Stupak for purposes of questions.

Mr. STUPAK. Thank you, Mr. Chairman. Mr. Timbers, in my opening statement I said we all share some responsibility here, and I stick with that statement. If we are going to share the responsibility, I guess I would pick up a little bit where Mr. Burr was.

I mentioned in my opening statement about Lee Iacocca coming here before Congress, actually this committee and Jim Blanchard was the Congressman from Michigan. And we helped out the Chrysler company, but Mr. Iacocca's salary was $1 and from what I have heard thus far today, it looks like your salary is about $1.2 million in cash not counting stock options where those values may be. It could very well be over $2 million. So if we are going to share this responsibility which I think we have to, if we are going to come and ask the Congress for a $200 million bail-out request, we have to all share in some of that responsibility.

When Congress privatized the USEC probably before any of us sitting on this dias, it is fair to say before any of us on this dias were in Congress, the purpose was to gain money for the Treasury; is that correct?

Mr. TIMBERS. Yes.

Mr. STUPAK. And, in fact, in 1991 you proposed privatization of USEC to the Bush administration; did you not?

Mr. TIMBERS. I am trying to think. In 1990, I worked for Smith Barney.

Mr. STUPAK. 1991 I said.

Mr. TIMBERS. I am not sure what you are referring to in 1991. There was proposals in another endeavor that I had.

Mr. STUPAK. Did you propose privatization of USEC to the Bush administration, you personally?

Mr. TIMBERS. If there was a proposal being made at that time, it was in the context of a report prepared under the company

Smith Barney; and I was acting on behalf of Smith Barney so if there was a proposal——

Mr. STUPAK. On behalf of the corporation, you recommended that USEC should be privatized?

Mr. TIMBERS. We recommended that the existing business of the uranium enrichment under the guise of operating within the full government had a great deal of difficulty for its future success. We recommended at that time that it would be——

Mr. STUPAK. Let's fast forward. I think the answer is yes that Smith Barney recommended it. You were part of that group. Let's go to 1998. In 1998 you supported, in the clearest terms, privatization of USEC through a public offering; did you not?

Mr. TIMBERS. I am sorry, did I——

Mr. STUPAK. In 1998 did you support privatization of USEC through a public offering IPO in 1998?

Mr. TIMBERS. I was asked by the Federal board of directors to give my views as to what was the best way to privatize and in responding to these views indicated that I thought the best plan was to privatize it through an IPO in terms of getting—maximizing——

Mr. STUPAK. The answer is yes then.

Mr. TIMBERS. [continuing] maximizing the criteria set by Congress.

Mr. STUPAK. I am not trying to cut you off. I am down to 2 minutes so I am trying to get through some of these questions.

USEC agreed to all those constraints you talked about in your statement in 1998, did they not?

Mr. TIMBERS. Yes.

Mr. STUPAK. In fact, if you had thought it was not workable, you would have recommended that privatization was not feasible; would you have not?

Mr. TIMBERS. That is correct.

Mr. STUPAK. But you didn't do that. You thought it was feasible, and you recommended in 1998 that they move forward?

Mr. TIMBERS. I did, yes.

Mr. STUPAK. According to the minutes of the board meetings in June and July 1998, you knew the market price of the SWU in new contracts was below your production costs and even below what you are paying for the Russian SWU and the price of that SWU would go up even if the market price went down. In fact, on page 44 of the minutes of July 22, 1998, the board is told that the average price of new contract is already below $90 an SWU, and there was concern reported in the press that it would go as low as 80 which would be the low production cost and the cost of Russian SWU. So you already knew that when you made these IPOs, right?

Mr. TIMBERS. I don't believe those were my observations, but I would like to go back and check the record.

Mr. STUPAK. June and July board minutes of 1998, I guess that was also based upon something from J. P. Morgan; right?

Mr. TIMBERS. Mr. Stupak, I would have to check the record on that.

Mr. STUPAK. In the book right there, I believe it is document number 22.

Mr. TIMBERS. This is my book.

Mr. STUPAK. Do we have document number 22 there we could show the witness. The same white book, wrong contents.

Under document number 22 it is on page 44. I stand corrected. Document 27, page 44 I am looking at—the second issue, on line 14, the second issue was the falling of new contracts below $80 per SWU. The intent at the time it was agreed to was not the very next contract you signed. This became a major issue because there was some concern that as you all know, the prices have been falling and the average price of new contracts has been heading below $90. There was some concerns stated in the press that it would be as low as 85, 84, and $80 would be breached within the next year.

So is that correct? That is what I am really trying to get at. And that's your board minutes.

Mr. TIMBERS. Mr. Stupak, I was not on the board of directors. And as I look at this document, this is the July 22, 1998 meeting; if I see the attendance, I was not present at that meeting.

Mr. STUPAK. So you were not at the meeting, but you were the CEO of the company?

Mr. TIMBERS. The Federal board of USEC did not have the CEO on the board. There are five Presidentially appointed, Senate confirmed members. That did not include the CEO.

Mr. STUPAK. Okay. But you knew the price of your contracts, did you not?

Mr. TIMBERS. Do you know who was saying this? Because this is somewhat out of context.

Mr. STUPAK. Mr. Goldman.

Mr. TIMBERS. Mr. Goldman is an attorney?

Mr. STUPAK. Right. You know the price of your contracts; right? Yes or no? Did you know the price of your contracts?

Mr. TIMBERS. Yes, I knew the price of the contracts.

Mr. STUPAK. So that is correct? That is the prices that you thought it would be?

Mr. TIMBERS. No, I believe that the contracts prior to privatization were approximately about $92 that were being added to the book. It says here there is some concern in the press that things would go lower. That is not necessarily what our view was at that time.

Mr. STUPAK. You are saying that you thought the new contracts were $92?

Mr. TIMBERS. I believe they were $92, which is higher—if I can refer to your statement, that is higher than the price we were paying to Russia.

Mr. STUPAK. Correct.

Mr. WHITFIELD [presiding]. Mr. Stupak, you have run over by about 2 minutes. If you could make this your last question.

Mr. STUPAK. Would you provide us some evidence that you knew it would be $92?

Mr. TIMBERS. In our disclosure documents, in terms of both the prospectus and the offering memorandum that we provided to potential bidders, I believe the price on there was $92 per SWU, to the best of my recollection. But I would be glad to go back and check that for the record, Mr. Stupak.

Mr. STUPAK. And you projected out that they would be $92? Would be your projected cost?

Mr. TIMBERS. We projected that the price would be stable at that time.

Mr. STUPAK. Really, even though the newspaper and everyone else said everything was going, if I can use the word, "to hell in a hand basket" in a big hurry. You had excess production capacity——

Mr. TIMBERS. I'm not exactly sure.

Mr. STUPAK. [continuing] of a uranium stock.

Mr. TIMBERS. Pardon me?

Mr. STUPAK. Everyone was saying that, look, excess production capacity, yet falling prices and liquidation of uranium stocks. The newspapers was saying it was going to be down in the low 80's, but still you projected out to the 90's and $92 in the future?

Mr. TIMBERS. We believed at that time that the market would be stable in terms of the pricing. The pricing that has dropped since privatization, as I indicated, which is about 15 percent, is a level that dropped the prices below a level that we were projecting at that time.

Mr. STUPAK. Mr. Chairman, thank you for the extra time.

Mr. WHITFIELD. Okay, I will ask questions next. Mr. Timbers, in the strategic plan that was developed in preparation for privatization in document 5 in the book you have a page with key assumptions on estimated new sales prices for SWU. In the year 1999, the estimated new sales price for SWU is $95 per SWU. And it show it's going up to $110 per SWU in the year 2007.

Mr. TIMBERS. With escalation. That includes escalation.

Mr. WHITFIELD. Now, we're talking about new sales; we are not talking about old contracts.

Mr. TIMBERS. That's correct.

Mr. WHITFIELD. And SWU never did reach any of these prices during these years, did it? I mean, right now you are selling them at about $80 a SWU.

Mr. TIMBERS. That's correct.

Mr. WHITFIELD. So where did these numbers come from that would show a projection of $95, $96, and $98 a SWU?

Mr. TIMBERS. The strategic plan in 1997. Obviously, market factors have changed since that time.

Mr. WHITFIELD. And what year did you prepare the strategic plan? 1997?

Mr. TIMBERS. Yes.

Mr. WHITFIELD. So things dramatically changed. Instead of having SWU at $95 in 1999, it is down to around $80.

Mr. TIMBERS. Things have considerably changed. There has been a fundamental change in terms of competitor pricing. There has been a contraction of the marketplace. There has been aggressive liquidation of inventories by customers here and abroad. And since this time period, the market is fundamentally different, even within the short period from September 1997.

Mr. WHITFIELD. So for whatever reason, the strategic plan is wrong on the SWU price.

Mr. TIMBERS. Well, anytime you develop a strategic plan, a strategic plan dynamic document, it is appropriate at that time——

Mr. WHITFIELD. Let me ask you another question. You have been with USEC since 1993?

Mr. TIMBERS. Yes.

Mr. WHITFIELD. And during that time that you have been associated with USEC, there has been a lot of discussion about AVLIS technology. Now in the board meeting on June 3, 1998, there was quite a bit of discussion about AVLIS technology in the context of which offer, IPO, merger and acquisition, would be the best way to go. And I know that Mrs. Green on page 253 made the comment: If you don't invest in AVLIS, there really is no future for enrichment. And on page 244, you said that every day that privatization is delayed, we delay the deployment of AVLIS. And then you said the No. 1 thing for the privatized company within the first 90 days is to begin the siting process for AVLIS. Technology is not the question, it is a siting delay.

And then in the prospectus, they talk about the competitive advantage of this company is the AVLIS technology. And it says that USEC plans to complete the development and commence commercialization of the next generation of uranium enrichment technology, AVLIS, and that it will be deployed at full-scale facility by 2005.

Now that was in 1998. What changed that made you all drop the AVLIS technology so completely after it had been sold as the technology that could make this industry succeed?

Mr. TIMBERS. AVLIS, prior to their privatization for a period of about 18 months, had a significant string of successes of demonstration performance at the Lawrence Livermore lab, and that gave us a considerable degree of confidence that the technology was being proven to be successful and that we can move to the level of deployment. And if you recall, subsequent to privatization, we began a deployment process where we began to make inquiries throughout the United States about possible sites, including Paducah and Portsmouth.

Now, what really has happened—what happened since that time is the technology did work. AVLIS technology did work, did enrich uranium. But what happened is that we could not get the further development in terms of longevity of operations of the enrichment process such that, as we tried at the Lawrence Livermore labs, the rate of return that we could get out of the project could not exceed the double digits.

Economically, we could not make this thing work from an investment standpoint. Technically, it worked. Technically, it reflected the results that we had, but we could not improve it to the point of making it economic.

Can I just explain how that works? In order to run AVLIS successfully, it had to run for a long period of time so that between a refurbishment module and what happened during our testing, subsequent to our good string of 18 months of tests, is that we could not extend that period sufficiently enough to get a great—a run rate of return on material that we were enriching.

Mr. WHITFIELD. So basically, the technology works but from a commercial standpoint, the return is simply not there?

Mr. TIMBERS. It did not work well enough.

Mr. WHITFIELD. Now, let me ask you, your production costs are in the $90 range using gaseous diffusion. You are selling SWU at $80. AVLIS technology does not work. So what's the answer?

Mr. TIMBERS. I've indicated in public disclosure and a number of different forums that we're looking at a two-pronged approach in terms of looking at acquiring centrifuge technology and also the R&D development of the Silex technology in Australia. Acquiring centrifuge technology can be either directly in reinstituting the DOE technology in Oak Ridge—and we are in discussions with DOE about doing that—and No. 2, it could be acquiring centrifuge technology from a European producer or from the Russians.

Mr. WHITFIELD. Now there are many independent analysts who say that because of the downgrading of the credit rating of USEC that it would be difficult for USEC to raise the money to pay for installing centrifuge technology.

Mr. TIMBERS. If there is an appropriate technology that is economic, I believe the money can be raised for it.

Mr. WHITFIELD. Okay. I see my time has expired. Mr. Strickland.

Mr. STRICKLAND. Thank you, Mr. Chairman.

Mr. Timbers, do you recall a meeting in Senator DeWine's office where Senator Voinovich was present, I was present, as well as members of our staff, when you said that it took a private corporation to be able to stop investing in AVLIS and that a government corporation would never have been able to do that? Do you recall that conversation?

Mr. TIMBERS. I recall the meeting, but I don't recall that conversation.

Mr. STRICKLAND. I think our staffs recall it very clearly. And I think I recall you saying in that meeting that when you first came on board, or early when you came on board USEC, that you said we ought to stop and take a look at this technology before we continue to invest in it.

The reason I think that is relevant is this: I assume the investors who bought stock in this private corporation rightfully believed that AVLIS was a viable technology that held out great promise to this industry. And I am wondering if those who bought the stock may feel just a little misled if, in fact, that was your feeling prior to the time of privatization. If you do not recall that conversation, then I'll accept that response, but I recall it clearly. And I think the two Senators do.

Mr. Timbers, do you remember requesting a waiver to allow you to participate in the privatization process?

Mr. TIMBERS. There was a series of waivers that were requested by the chairman of the board to waive government ethics issues.

Mr. STRICKLAND. You say they were requested by the chairman of the board?

Mr. TIMBERS. Yes.

Mr. STRICKLAND. I have a letter here from the chairman of the board to you, and it says: On September 25, 1995, you provided me with a request for a waiver under section 208(b)1 to allow you to participate in matters directed toward the implementation of the plan of privatization of the United States Enrichment Corporation. Your request——

Mr. WHITFIELD. Mr. Strickland, would you care to introduce those into the record?

Mr. STRICKLAND. I would. This waiver letter, it is dated September 26, 1995, from Mr. Rainer.

He further says: Your request stated that such matters would include—and I won't list all of them—but one of things that you requested was to be able to participate in the method that USEC should utilize in privatizing; e.g., an IPO or an M&A transaction. You also requested to be able to participate in the selection of individuals to be appointed to serve on the board of the privatized corporation. And I think that may be relevant to the discussion about whether or not there had been a discussion of whether or not your compensation was on the board—was on the table, since you had great influence, apparently, in the selection of the board.

But the law says, and i quote from the law, under Title 18, Crimes and Criminal Procedure of the United States Code section 208 A, "Whoever, being an officer or employee of the executive branch of the U.S. Government or of any independent agency of the government, participates personally and substantially as a government officer or employee through decision approval, disapproval, recommendation, their rendering of advice, investigation, or otherwise in a contract claim controversy or other particular matter in which he has a financial interest shall be subject to penalties set forth."

But then Mr. Rainer says, given the scope—given these factors and the scope of this waiver as delineated herein, I do not find your disqualifying financial interest to be so substantial as to be deemed likely to affect the integrity of your service to the government.

Now, we have heard here today that your salary went from $350,000, approximately, to perhaps over $2 million. I don't know what you or Mr. Rainer would consider substantial. To me, that is incredibly substantial. And so it seems as if you were intimately involved in these decisions regarding how to privatize, the selection of the board members for the new corporation, and it troubles me greatly that I think the—certainly the intent of the law, the intent of the law was not carried out in this procedure.

And it calls into question whether or not all of the decisions that were made between you and the board and the Department of Treasury were decisions that were made in the best interest of this country or if they were made to further the personal financial interests of those involved.

It is a troubling set of circumstances, and as we move forward I think it is appropriate that we look at where we have been, because we need to know who and what it is, Mr. Chairman, that we are dealing with as we look forward to the future of this industry. And with that I yield back my time.

Mr. WHITFIELD. Mr. Bilbray.

Mr. TIMBERS. Mr. Chairman, if I could actually make one comment. I appreciate Mr. Strickland bringing parts of that letter to my attention. I had forgotten the procedures about who requested what waiver process, so that I stand corrected by Mr. Strickland identifying those who requested. I just did not recall.

Mr. WHITFIELD. Mr. Strickland—Mr. Bilbray.

Mr. BILBRAY. Mr. Chairman, how many times have you been to Mr. Strickland's Ohio or Mr. Whitfield's Kentucky facility?

Mr. TIMBERS. Dozens of times. I have had board meetings there both in the private and in the government corporation.

Mr. BILBRAY. Have you been to the plants to see the operations themselves?

Mr. TIMBERS. Dozens of times.

Mr. BILBRAY. How long ago was the last time you were there.

Mr. TIMBERS. About a year ago at both plants. I've had board meetings—I took the private board to a board meeting at both of the plants over the past year.

Mr. BILBRAY. But when you talk about—it has been a year since you have actually seen the operation in the plants?

Mr. TIMBERS. The last visit was the board meeting that we had which was in approximately—about a year ago.

Mr. BILBRAY. Now, the board meeting, I'm just trying to see as the CEO of the corporation, what was the last time you were in and actually witnessed the operation itself at those plants?

Mr. TIMBERS. I do not have the date, Mr. Bilbray, but the date that board meeting was, we saw the operations of the plants. If you have a board meeting there, you conduct business, but the primary reason is to have the board view the plants, take a tour of the plants, talk to management and talk to workers.

Mr. BILBRAY. So it has been a year since you have been at the physical plants?

Mr. TIMBERS. Approximately that. Whenever date that board meeting is.

Mr. BILBRAY. Thank you. I appreciate that. Mr. Chairman, I yield back.

Mr. WHITFIELD. We have a vote on the floor. I want to ask one other question. Mr. Strickland, do you have any additional questions for Mr. Timbers?

Mr. STRICKLAND. Mr. Chairman, could we submit questions to have answered in writing?

Mr. WHITFIELD. Yes, without objection, so ordered.

Mr. STRICKLAND. Thank you, Mr. Chairman.

Mr. WHITFIELD. I have one other question. Mr. Timbers, in the past several days, my office has been receiving a lot of fax letters from employees at USEC. They are blaming the Nuclear Regulatory Commission, or at least stating that in the new criticality safety standards which they say are delaying your efforts to certify the Paducah plant for a high assay upgrade, that the NRC is using different standards at Paducah than they are using at the Piketon plant.

However, according to a letter we received from the NRC, they say the reason why your announced plans to get the high assay upgrade approval by the end of the year won't take place is because USEC has failed to follow the proper documentation in a timely manner. Do you have any comment about those letters?

Mr. TIMBERS. I'm not aware of those letters. If there is a difference in terms of the views about what is corporate criticality safety, I will be glad to look into it, but I am not aware of what those letters are referring to.

Mr. WHITFIELD. You are not aware of the letter from the NRC saying that USEC has not filed its documentation in a timely manner and that the information that you have provided is incomplete and not factual?

Mr. TIMBERS. I'd like to go take a look at that letter.

Mr. WHITFIELD. It is in document 18 of the book.

Mr. TIMBERS. It is in 18?

Mr. WHITFIELD. It is a letter addressed evidently to Steven Toelle.

Mr. TIMBERS. This is about the financial review conducted by the NRC? The letter I'm pointed to is March 29, 2000, regarding USEC financial evaluation. Is that the letter?

Mr. WHITFIELD. Just a minute. I tell you what we'll do, we will get that to you in writing as well. And a copy of the letter.

Mr. TIMBERS. Be glad to answer that Mr. Chairman.

Mr. WHITFIELD. As soon as we get back from voting we will call up the second panel. I understand we have a vote in about 5 minutes and then we are going to have another 5-minute vote and then we will be right back.

But, Mr. Timbers, in concluding I would simply say that production costs are up in the $90 range and you are selling SWU around $80. Your old contracts were around $110 a SWU. AVLIS is off the table. We don't know if centrifuge is going to work or not. Many people are concerned that you are buying back stock and that the long-term viability of USEC is in danger. And that's one of our primary concerns and that's why we are looking forward to additional testimony today from other people who have analyzed it. But I want to thank you for coming today. We appreciate your being here. And there may be some additional questions that we would like to submit to you in writing.

Mr. TIMBERS. That would be fine.

Mr. WHITFIELD. Thank you.

Mr. TIMBERS. Mr. Chairman?

Mr. WHITFIELD. Yes?

Mr. TIMBERS. There are two submissions—there were two points I would like to make, just before we adjourn for a moment, in answering Mr. Stupak's question about the trends toward lower pricing. And he was inquiring about what our views were at the time of privatization. We would like to submit for the record page 13 of our offering prospectus in 1998 that talks specifically about our disclosure on trends toward lower pricing. And the second point—if that meets with your approval.

Mr. WHITFIELD. That's fine.

Mr. TIMBERS. The second point is that, gee, my salaries were mentioned a couple of times and Mr. Stupak has mentioned that it is $1.2 million. My salary is $600,000, as I stated. The balance of the compensation is at risk.

Mr. WHITFIELD. Page 13 is already in the record of your prospectus. So we've got it.

Mr. TIMBERS. Okay.

Mr. WHITFIELD. Thank you very much. As soon as we come back, we are going to call up panel II——

Mr. STRICKLAND. Mr. Chairman, could I ask another question? And I'll be happy to miss the vote in order to ask this question.

Mr. WHITFIELD. Sure, go right ahead.

Mr. STRICKLAND. Thank you. Mr. Timbers, there has been speculation that in order to reach one of the significant events necessary to enable USEC to close one of the two plants before their obligation ends in 2005, that there has been some manipulative behavior

on the part of USEC which would enable them to reach a significant event.

In fact, Morgan Stanley has written this: With aggressive stock buy-backs, the debt could be downgraded to below investment grade. That would be a formal condition allowing USEC to shut down one of the unneeded production plants which would save $100 million annually, according to management. But the physical—the physical capacity to do all needed production at one plant may be a year or more away, and there will be heavy political pressure fighting any such shutdown.

Are you aware of Morgan Stanley's suggestion?

Mr. TIMBERS. I think I do. My best recollection is I do recall a statement like that.

Mr. STRICKLAND. And were you aware of this recommendation prior to the decision to buy back the stock?

Mr. TIMBERS. I don't know the date of that recommendation. The decision to buy back the stock is independent. You know, you're making, I think, a connection between a significant event under the Treasury agreement and the stock buy-back. In February we announced three major actions by the corporation. One was the announcement that our earnings for fiscal year 2000, beginning in July of this year, would be about 60 percent below this year's earnings. No. 2, we announced a stock buy-back. And No. 3, we cut the dividend by one-half.

What I would like to point out is that the amount of money that the corporation saved by cutting the dividend by one-half is about equivalent over this period of time to the amount of money that would be used for a stock buy-back program if completed.

I would note very carefully that if there was an intention by anybody in regard to—by the rating agencies in regard to these three announcements, the reduction of earnings by 60 percent was the most dramatic element that the rating agencies would pay attention to.

Mr. WHITFIELD. Mr. Strickland, I am going to have to ask to you finish up. I need to make this vote, even though you may not.

Mr. STRICKLAND. Your December 1999 quarterly report lists all of the things that could occur that would enable one of the plants to be closed.

Mr. TIMBERS. I think we have listed that in a number of different quarters, not just that one quarter.

Mr. STRICKLAND. On February 4, 2000, Standard & Poors revised its credit rating of USEC's long-term debt to below investment grade. It troubles me that there appears to be perhaps a manipulative behavior on the part of the corporation which would enable them to violate an agreement which they have had, a legally binding contract with the Department of Treasury. And when we talk to Mr. Gensler, I'm going to ask him if he is aware of any such behavior and what the action of the Department of Treasury will be in response.

Mr. TIMBERS. Mr. Strickland, that view is not accurate. And it is not accurate about the conduct of the company.

Mr. WHITFIELD. Thank you very much, Mr. Timbers. We will be right back.

[Brief recess.]

Mr. WHITFIELD. I will call the meeting back to order. We have the gentlemen from panel II, the Honorable Gary Gensler, Under Secretary, United States Department of Treasury, we appreciate your being here very much. Mr. Ernest Moniz, Under Secretary, Department of Energy, we appreciate your being here. And Mr. Carl Paperiello, Deputy Executive Director for Materials Research and State Programs the U.S. Nuclear Regulatory Commission. Thank you for being here.

With that, Mr. Gensler, if you would like to proceed with your opening statement. And, of course, the entire statement will be submitted for the record.

TESTIMONY OF GARY GENSLER, UNDER SECRETARY, U.S. DEPARTMENT OF TREASURY; ERNEST J. MONIZ, UNDER SECRETARY, U.S. DEPARTMENT OF ENERGY; AND CARL J. PAPERIELLO, DEPUTY EXECUTIVE DIRECTOR FOR MATERIALS, RESEARCH AND STATE PROGRAMS, U.S. NUCLEAR REGULATORY COMMISSION

Mr. GENSLER. I thank you, Mr. Chairman, ranking member. I appreciate your calling this hearing. I know this is a very important matter to the Congress and very important to you and your district and Congressman Strickland's district, and we take these matters very seriously at Treasury and throughout the administration.

I'd like to just summarize my remarks and I appreciate submitting them for the record.

The statutory framework for the privatization of USEC was laid out in two important acts by Congress in 1992 and in 1996, best recollection. Throughout the privatization process we followed the statutory framework provided by Congress closely, thoroughly, and conscientiously. Between those two acts in 1992 and 1996, the U.S. Government entered into a very important arrangement with the Russian Federation as it related to the sale of the bomb grade material out of Russia, known as the HEU Agreement.

The President had submitted to him a privatization plan, the same plan that Congress considered in 1996. That plan was submitted to the President and the President signed off to the privatization plan in 1997, which considered what was called a dual-path process. And as you most likely recall, this is a process whereby outside financial experts, working with the USEC board of directors, would look and explore the sale by merger and look and explore the sale by the initial public offering.

The most attractive third party proposal, if I could just highlight this, and this is much more detailed in the public record and in my prepared remarks, but the most attractive third party sale proposal was a leveraged buyout. And just to pause for a moment, the USEC searched with 50 companies to see if there was an interest in buying the company. What was found is that there was a limited interest in the purchase of the company by large commercial firms. There was more of an interest by financial parties through what's called a leveraged buyout, and in fact those were the only two proposals received. This put a significant amount of leverage on the company, approximately $1.5 billion of fixed rate securities, and then had investors in the equity.

The USEC board determined that both the proposed sale transaction, this leveraged buyout transaction, and the public stock offering satisfied the statutory criteria that Congress had laid out. But they concluded that the offering was the best of the two alternatives.

Treasury's role was then to take an extensive review of USEC's board decision, based upon all the available information at the time. As part of this review it sought and obtained advice from over a dozen Federal agencies with regard to the statutory criteria laid out by Congress. And I would say that it was a very complex set of circumstances. As many commercial firms are, USEC is also complex, but the statute itself had many criteria that we sought to review.

In coordinating that interagency process, all the essential decisions that were made on the privatization reflected a collective judgment of the appropriate government agencies, whether it be national security issues, the very important issues of labor and the environment, very important issues of the continuation of the plants.

Mr. WHITFIELD. May I interrupt you just a minute Mr. Gensler. I have just been reminded, which I should have remembered at the beginning, this is an oversight hearing. We would like to ask you, unless you have some objection, to stand and be sworn that what you are testifying to will be the whole truth and nothing but the truth. All witnesses, if you would raise your right hand.

[Witnesses sworn.]

Mr. WHITFIELD. Thank you very much. Now we're sworn in.

Mr. GENSLER. I appreciate that. I always assume, if I am in front of Congress, that to be the case.

In consultation with the other agencies, Treasury determined that both the public offering and the merger path met the statutory criteria but determined the offering was best in meeting those statutory criteria. And while I detail it more in the testimony, this involved at least four areas: expected level of debt—the leveraged buyout, as I said, had close to three times the amount of fixed rate obligations, and two, the higher level, at least initially, of employment. The leveraged buyout was suggesting as many as 1,700 layoffs and the initial public offering, in the order of 500 layoffs. And we were able to at least memorialize for 2 years in the Treasury agreement higher expected proceeds and lower expected market and financing fiscal risks.

Additionally, I would note in the terms of the level of debt and long-term viability, the credit rating by independent credit rating agencies came in at what's called triple B plus, which was higher than the level that would have been in the leveraged buyout of only triple B rating, both of which were above the minimum rate that the NRC, who I know probably will be commenting later, had initially laid out in their draft standard review plan.

To address many of the concerns raised by Congress, there were numerous arrangements with USEC during the privatization and post privatization. And just highlighting them briefly, on the national security side there were numerous arrangements with the State Department, of course, the Enrichment Oversight Committee,

the Department of Energy and the NRC, a very important issue as we all know today.

There is the certification process with the NRC itself, and I would of course defer to the NRC, but those standards in terms of compliance with health and safety standards, compliance with very important issues as laid out by Congress. Labor and environmental issues. Very importantly, many agreements were entered into with the Department of Energy and following up also in agreements with the OMB.

Treasury did not have any explicit requirement in the statute beyond privatization, but we thought it was appropriate to enter into a contractual arrangement to best forward the statutory criteria as laid out by Congress. And that agreement I think is, as you know—had four specific arrangements for post privatization. One related to the compensation levels of the private firm after privatization. The second was the labor component with regard to the 2 years for the 500 employees. Third, it related to the sale of assets. The statute actually said that this company could not sell more than 10 percent of its stock for 3 years, consistent with that we embodied that about assets. And fourthly and very importantly with regard to the plants, continued operation of the plants through January 2005, unless the actual viability of the company in some way was in question through a significant event. A significant commercial event was defined as either a significant decline in earnings, pricing, operating results or, as is somewhat focus in this hearing, loss of the investment grade rating.

Treasury has vigorously enforced this agreement. Just as one example, subsequent to the privatization, USEC management attempted to renegotiate the restrictions on the layoffs. Treasury did not allow this and thought very carefully but very clearly that we should not deviate from those obligations. In addition, earlier this year in January when we first heard that the board may be considering something with regard to the plants, we requested that the company notify Treasury immediately if they were considering such a closing. We asked for ample time to review and the legal justifications of any considerations the board may have in this regard.

I would note for the record that USEC has not notified us to this day that they see that there has been such an event or that they are taking such actions. While there is no statutory basis for ongoing Treasury oversight of USEC, we take our role with regard to that contract very seriously. And despite our limited role, we also feel that we must be and should be responsive to this Congress with regard to these matters.

Mr. WHITFIELD. If you could summarize for us, Mr. Gensler.

Mr. GENSLER. I was actually done, so that was perfect timing.

[The prepared statement of Gary Gensler follows:]

PREPARED STATEMENT OF GARY GENSLER, TREASURY UNDER SECRETARY

Mr. Chairman and members of the Subcommittee, I appreciate the opportunity to testify on the privatization of the United States Enrichment Corporation ("USEC"). The privatization of USEC was the culmination of a process mandated by Congress through the enactment of the Energy Policy Act of 1992 and the 1996 USEC Privatization Act. Throughout the entire privatization process, we followed the statutory framework provided by Congress very closely, thoroughly, and conscientiously.

I will divide my remarks into five parts: first, a general discussion of the statutory framework on which the privatization process was based; second, a discussion of the

privatization decision of the USEC board of directors (the "USEC Board"); third, a summary of the governmental review of the USEC Board's decision and reasons the government agencies approved the public stock offering as the best means of achieving privatization; fourth, the measures taken by the federal government relating to USEC's conduct during and after the privatization; and fifth, Treasury's involvement in USEC-related matters following privatization.

STATUTORY FRAMEWORK

The process that culminated in the privatization of USEC was begun by Congress in 1992, when it enacted the Energy Policy Act. That legislation established USEC as a government corporation and gave it a mandate to develop a strategic plan for privatization. The 1992 Act set up a board of directors that was composed of members appointed by the President and confirmed by the Senate.

The 1992 Act authorized USEC to implement its privatization plan upon the occurrence of two events. First, the President had to approve the plan. Second, the USEC Board had to determine, in consultation with appropriate agencies of the United States, that privatization would satisfy four statutory criteria: a return to the United States at least equal to the net present value of USEC as a government corporation; protection against foreign ownership, control, or domination of USEC; protection of public health and safety and common defense and security; and a reasonable assurance of adequate enrichment capacity to meet the demand of the domestic electric utility industry.

In 1996, before the President had approved USEC's privatization plan, Congress again passed legislation aimed at prompting the sale of USEC. The USEC Privatization Act established additional requirements for the certification and licensing of USEC's uranium enrichment activities by the Nuclear Regulatory Commission ("NRC") and contained provisions to clarify the allocation of assets and liabilities between the government and a privatized USEC, including a section that provided for the transfer of substantial quantities of natural and enriched uranium from the Department of Energy ("DOE") to USEC. The 1996 Act also enacted protections for USEC's workers, including a requirement that DOE provide benefits to certain USEC workers in the event of a plant closing or mass layoff.

Finally, the 1996 Act directed USEC to privatize, with the approval of the Secretary of the Treasury, in a manner that satisfied the additional statutory criteria of providing for: the long-term viability of USEC, the continued operation of the gaseous diffusion plants that USEC leases from DOE, and the maintenance of a reliable and economical domestic source of uranium mining, enrichment, and conversion; and, to the extent not inconsistent with these three criteria, obtaining the maximum proceeds for the United States.

THE USEC BOARD'S DECISION

First Steps

In 1995, USEC submitted its plan for privatization to the President and Congress. The plan accomplished the statutory requirement to evaluate alternative means of privatization by establishing a "dual-path" process, in which USEC simultaneously prepared for an initial public offering of stock and a negotiated sale to a third party. The plan concluded that such a dual-path process would allow decision-makers to select the best means of privatization on the basis of concrete information about the relative merits of specific transaction alternatives. In July 1997, the President approved the privatization plan subject to the development of an adequate post-privatization oversight process.

Third-Party Sale

To initiate the negotiated third-party sale path of the dual-path process, USEC's transaction manager distributed over 50 preliminary information packages to industrial, utility and financial firms. USEC received expressions of interest from five parties. The USEC Board reviewed these submissions and consulted with the appropriate federal agencies for national security clearance of the interested parties. Based on its review, the USEC Board invited three of the parties to conduct due diligence at USEC's facilities. After extensive due diligence by the interested parties, USEC received two firm proposals for the acquisition of USEC through a negotiated third-party sale. Interested parties were directed to submit an extensive package of information, including a firm, all-cash proposal; a definitive mark-up of a draft merger agreement; binding financial arrangements; strategic business plans for the privatized corporation; comprehensive disclosure on their consortium arrangements, including charter documents and shareholder agreements; regulatory

information; and information on how the interested party would satisfy the statutory criteria of the privatization legislation.

Public Stock Offering

Simultaneous with the third-party sale path, the USEC Board and USEC's management worked with their financial and legal advisors to prepare for a possible public stock offering. The involvement of private sector financial and legal advisors in transactions of this nature is necessary and standard, and we believe their involvement contributed greatly to the decision-making process. Once the USEC Board procured the services of these advisors, USEC worked with them to prepare the necessary Securities and Exchange Commission registration statement. The advisors also provided advice on the timing of a stock offering and valuation range, and coordinated appropriate marketing efforts, including road shows.

In addition, USEC's advisors each provided independent advice on the appropriate levels of debt that USEC should incur to maximize value for the federal government. These financial advisors concluded that incurring a reasonable amount of debt prior to an offering would increase the gross proceeds to the federal government, reduce the aggregate amount of fees paid to financial advisors, and reduce the amount of proceeds subject to market risk. The inclusion of debt in connection with an initial public offering is a standard financing practice that is utilized in privatizations around the world. Upon review of those analyses, Treasury and OMB agreed that the USEC financing structure, in the event of a public stock offering, should include net debt of $500 million. The financial advisors advised Treasury that this net debt would not affect the long-term viability of the privatized corporation.

The Decision

The USEC Board considered third-party sale proposals from two potential buyers. The most attractive proposal (the "Carlyle proposal") was a leveraged buy-out that offered $1.9 billion for the acquisition of USEC, subject to a number of conditions. The second third-party sale proposal was also a leveraged buy-out, but it offered less attractive terms than either the Carlyle proposal or the public stock offering proposal.

On June 11, 1998, the USEC Board determined that both the Carlyle proposal and the public stock offering proposal satisfied the statutory requirements, but that the offering provided the superior method of addressing the special areas of concern identified in the two privatization statutes. The USEC Board unanimously approved privatization through the public stock offering.

GOVERNMENTAL REVIEW OF THE USEC BOARD'S DECISION, AND REASONS FOR APPROVING THE PUBLIC STOCK OFFERING

Governmental Review Process

During the entire privatization process, judgments were made collectively by the appropriate agencies of the Administration. Treasury coordinated this inter-agency process. To ensure that the views of the appropriate agencies were taken into account, during the entire dual-path process Treasury consulted extensively with such agencies as the Council of Economic Advisors ("CEA"), the Central Intelligence Agency ("CIA"), the Department of Commerce ("DOC"), the Department of Defense ("DOD"), DOE, the Department of Justice ("DOJ"), the Department of State ("DOS"), the National Economic Council ("NEC"), NRC, the National Security Council ("NSC"), and the Office of Management and Budget ("OMB"). All of the essential decisions made during the privatization process reflected the collective judgment of these government agencies.

As part of our review of the USEC Board's decision to approve the public stock offering as the method of privatizing the corporation, we sought and obtained advice from federal agencies having expertise relevant to the statutory criteria specified by Congress in the two privatization statutes. Specifically, we obtained advice in writing from: (1) DOE on the satisfaction of the statutory criteria related to long-term viability, continued operation of the enrichment facilities, and a reliable and economical domestic source of uranium mining, enrichment and conversion services; (2) DOC and NRC on the satisfaction of the statutory criterion related to reliable and economical domestic source of uranium mining, enrichment and conversion services; and (3) OMB on the satisfaction of the statutory criterion related to securing maximized proceeds to the United States. The consultative process included extensive discussions with senior representatives from DOE and OMB.

In addition, Treasury asked the CIA, DOD, DOE, DOS, the Federal Bureau of Investigation, NRC, NSC, and OMB to provide any information about the members of the parties (and their affiliates) that submitted final third-party sale proposals

that might, in the view of these agencies, have a material effect on the government's review of the proposals. None of these agencies informed Treasury of any information on this subject. Finally, the NSC was fully involved throughout the privatization process and chaired a number of meetings on national security-related matters. The NSC, in consultation with appropriate national security agencies, determined that the privatization plan was consistent with the national security requirements of the statutes.

In addition, staffs from Treasury and other agencies undertook an extensive review of the available information, including the following: (1) written materials and oral presentations provided by USEC's management on the Corporation, its strategic plans, and the uranium enrichment industry; (2) proposals received from the parties interested in the acquisition of USEC through a negotiated third-party sale; (3) written materials from, presentations by, and discussions with USEC's financial and legal advisors, including a formal written opinion from its financial advisor; (4) four meetings of the USEC Board on the method and manner of sale (which included meetings with each of the parties interested in a negotiated third-party sale, union representatives, and a Congressional representative); (5) discussions with the leading candidate for a negotiated third-party sale regarding its proposal; (6) "bring-down" discussions and presentations by the financial advisors; and (7) discussions with the Oil, Chemical, and Atomic Workers Union.

Reasons for Approving the Public Stock Offering

Treasury determined that both the public stock offering and the Carlyle proposal met the statutory criteria for privatization, but that the offering was the superior method of addressing the special concerns identified in the privatization legislation. The primary reasons for our determination were a lower expected level of debt, higher expected levels of employment, higher expected proceeds, unresolved contract points with Carlyle, and lower expected market and financing risks.

Debt Levels/Credit Rating—The debt level under the Carlyle proposal would have been $1.2 billion, as compared with $500 million under the stock offering. In addition, the Carlyle proposal included about $355 million in preferred stock, which would have been a fixed-rate obligation. The actual credit rating under the public stock offering proposal was BBB+. This was higher than the expected credit rating under the Carlyle approach (BBB). The credit rating under the stock offering was also higher than the minimum level deemed acceptable by the USEC Board (BBB) for its statutory determinations. Also, as I will discuss later in this testimony, the credit rating under the stock offering was higher than the credit rating suggested by NRC as the minimum threshold for transfer of the certificate to the privatized corporation without further review of USEC's financial structure (BBB-). The reduced debt level and higher credit rating under the stock offering were key factors supporting the determination that privatization provided for the long-term viability of USEC.

Relative Impact on Employment—The Carlyle proposal included large, rapid reductions in employment at the two gaseous diffusion plants within the first two years of over 1,700 jobs (gross figure). The reduction would have been partially offset by plant reconfiguration and other activities, but the net decrease in employment over two years would have been about 1,400 jobs. In contrast, the public stock offering proposal included job reductions within the first two years of about 500, plus normal attrition.

Expected Proceeds—

The mid-point of the expected range of the estimated net proceeds from the public stock offering was approximately $40 million greater than the estimated net proceeds from the Carlyle proposal. Moreover, the estimated difference between the two approaches might have been even greater because the Carlyle proposal included the establishment of an escrow account of $100 million, which would be held aside for up to six years to indemnify Carlyle against certain contingencies. The escrow proposal created uncertainty as to the ultimate amount of net proceeds that would result from the Carlyle proposal. Carlyle also conditioned its proposal upon the issuance of a favorable determination from the Internal Revenue Service concerning the tax treatment of the proposed transaction.

Relative Financing Risks—USEC's transaction manager advised the government that, although there would be market exposure for the public stock offering during the marketing period of three to four weeks, the market risk was low. The Carlyle proposal, on the other hand, involved certain financing risks, as the commitment letters were subject to material market changes, equity investments by members of the Carlyle Consortium, due diligence, and other factors.

Restrictions During Privatization Process

During the privatization process, Treasury required that USEC take certain actions to protect the integrity of the process. Treasury insisted that the pre-privatization members of the USEC Board not continue with the privatized corporation and that the transaction manager be precluded from representing USEC for a period of two years after privatization. Treasury also insisted that only one member of USEC's current management serve on the board of directors of the privatized corporation, and not initially as the chairman, and that the privatized corporation's charter documents not contain "anti-takeover" provisions that might entrench management.

Agreements Governing USEC's Post-Privatization Conduct

The federal government negotiated a number of contracts with USEC that would govern the corporation's conduct after privatization to address special areas of concern reflected in the privatization statutes.

National Security—Since 1993, USEC had served as the United States Government's Executive Agent under the agreement between the United States and the Russian Federation concerning the disposition of highly enriched uranium extracted from nuclear weapons (the "Russian HEU Agreement"). In anticipation of the possibility of USEC's privatization, the President in 1998 established, by executive order, a federal inter-agency Enrichment Oversight Committee. Among other functions, this committee coordinates the government's monitoring of the privatized corporation's implementation of the Russian HEU Agreement.

Shortly before the privatization, USEC entered into an agreement with DOE under which USEC agreed that the privatized corporation would supply periodic information reports to DOE to support the functions of the Enrichment Oversight Committee. The privatized corporation has succeeded to USEC's rights and responsibilities under the agreement among DOS, DOE, and USEC guiding USEC's performance as the United States Government's Executive Agent under the Russian HEU Agreement. At DOS's request, Treasury also obtained a written statement from USEC indicating its intent to limit the amount of natural uranium that it would sell into the marketplace.

The National Industrial Security Program, which is administered by DOE and NRC, restricts foreign involvement in entities that require access to classified information. Because enrichment operations require access to classified information, the privatized successor to USEC must meet the requirements of this program. The program requires annual re-certification that the privatized corporation is free from foreign ownership, control, or influence that may result in the compromise of classified information. In addition, the privatized corporation has an ongoing responsibility under the program to report any changes in the nature or extent of foreign ownership, control, or influence.

Nuclear Regulatory Commission Certification—In the USEC Privatization Act, Congress gave the NRC ongoing authority to review USEC's compliance with three of the privatization criteria in connection with periodic NRC certification proceedings. Specifically, NRC must determine that (1) USEC is not subject to foreign ownership, control, or domination, (2) the certification of USEC would not be inimical to the common defense and security, and (3) the certification of USEC would not be inimical to the maintenance of a reliable and economical domestic source of enrichment services. NRC certification also focuses on health, safety, and environmental concerns. Under the statute, USEC or any successor corporation must apply for certification at least every five years.

To assist in implementing this provision, NRC staff prepared a standard review plan that described information to be examined and factors that it would consider in applying the three statutory criteria. For the criterion relating to a reliable and economical domestic source of enrichment services, the review plan provides that approval should be automatic if USEC or a successor corporation has an investment grade credit rating. An investment grade rating is generally considered to mean at least a BBB-rating. The NRC review plan also provides, however, that an applicant with a lower credit rating, or no credit rating at all, may receive certification if other factors support a favorable determination.

Labor and Environment—USEC entered into two agreements with DOE to ameliorate the effect of job reductions resulting from the privatization. USEC agreed with DOE in the first agreement that the privatized corporation would provide certain worker transition assistance benefits using an agreed-upon amount of USEC's pre-privatization funds. Under the second agreement, USEC agreed to pay DOE a certain amount of USEC's pre-privatization funds for DOE to assume responsibility

for a certain amount of depleted uranium produced by the privatized corporation, and DOE agreed to apply these funds in ways aimed at creating new jobs or giving hiring preferences to qualified laid-off workers.

With respect to environmental matters, USEC entered into an agreement with OMB allocating costs between the privatized corporation and the federal government for certain environmental liabilities.

In addition to the agreements concerning post-privatization conduct, the privatized corporation is subject to the Occupational Safety and Health Review Commission's worker health and safety regulations and the Environmental Protection Agency's environmental regulations.

The Post-Closing Agreement—Treasury also entered into a separate agreement with USEC a few days before privatization that limited the corporation's conduct after privatization. This agreement, entitled the Agreement Regarding Post-Closing Conduct (the "Post-Closing Agreement"), was not explicitly required by the statutes. Treasury felt, however, that this agreement was the best way to address special areas of concern identified in the privatization.

The Post-Closing Agreement imposed four main limitations on the corporation's conduct after privatization: first, restrictions on executive compensation; second, a two-year restriction on layoffs; third, a three-year restriction on a sale of all or substantially all of USEC's assets; and fourth, a restriction on plant closings until January 1, 2005.

On the subject of executive compensation, Treasury obtained USEC's agreement that the privatized corporation's executive officers would not receive any increase in salary for at least 180 days after the privatization and would not receive any stock options unless the plans under which they were granted were approved by the new shareholders. Treasury sought these agreements to protect the integrity of the privatization process.

On the subject of employment, Treasury obtained USEC's agreement that layoffs at the gaseous diffusion plants through the privatized corporation's fiscal year 2000 would not exceed 500, and that they would be conducted in substantially equal parts in fiscal years 1999 and 2000.

On the subject of asset sales, Treasury obtained USEC's agreement that the privatized corporation would not sell all or substantially all of its uranium enrichment assets or operations for a three-year period after the closing of the privatization. This provision in the Post-Closing Agreement was designed to complement a provision in the 1996 Act, in which Congress restricted any person from acquiring more than 10% of USEC's stock during the three-year period after privatization. The provision in the Post-Closing agreement was also designed to ensure that USEC's operations could not be sold off piecemeal by USEC during the period immediately after privatization.

On the subject of continuous operation of the plants, Treasury obtained USEC's agreement that the privatized corporation would continue to operate the gaseous diffusion plants until January 1, 2005, unless a "Significant Event" (as defined in the Post-Closing Agreement) occurs that could threaten the corporation's viability or the maintenance of a reliable domestic enrichment industry.

TREASURY'S INVOLVEMENT SUBSEQUENT TO PRIVATIZATION

Treasury has vigorously enforced the restrictions contained in the Post-Closing Agreement. For example, subsequent to privatization, USEC attempted to renegotiate the restriction on layoffs. Treasury, however, refused to allow USEC to deviate from its obligations under the Post-Closing Agreement.

In addition, earlier this year, Treasury sent a letter to the Chairman of USEC stating that we had been informed that the Board was about to consider the closure of a plant. In that letter, we referred USEC to the plant closing restrictions in the Post-Closing Agreement. We also stated that, as a party to the Post-Closing Agreement, Treasury has an interest in receiving information concerning proposed plant closings. Accordingly, we said that we would like to review and comment on the legal justification for any proposed plant closing prior to any meeting of USEC's Board of Directors which may consider such a closing.

Further, we requested that USEC notify Treasury immediately if it is considering a closing based on the occurrence of one or more Significant Events and that USEC provide the factual basis for concluding that a Significant Event has occurred or is likely to occur in the near future. We explained that it is important that Treasury has ample time to evaluate independently the merits of such a plan, so that we may verify USEC's adherence to the requirements of the Post-Closing Agreement.

Senior Treasury officials have met with members of Congress and their staffs to discuss USEC. Treasury has also attended meetings of the Enrichment Oversight

Committee since privatization. The meetings have focused on energy and national security issues. As a result, our participation in the meetings has been limited.

There is no statutory basis for ongoing Treasury oversight of USEC—which is now a private corporation—other than the Post-Closing Agreement. In addition, although USEC's operations involve important issues in the areas of national security, labor, and energy, these topics are outside of Treasury's area of expertise. Despite our limited role since privatization, however, we are committed to being as responsive as possible to concerns raised by Congress and others.

CONCLUSION

Mr. Chairman, we went to great lengths to fulfill the statutory direction for privatization in a manner consistent with the special areas of concern identified by Congress. Decisions at every juncture were the result of a careful, collective determination by the many federal agencies and organizations involved in the process. In entering into the Post-Closing Agreement, we believe we even went beyond the express requirements of the privatization statutes.

It's been almost two years since the privatization occurred. During such a timeframe, markets can change dramatically. Global and domestic economic conditions can shift considerably. Private sector firms must continually make business decisions in order to compete in a changing market environment.

At the time of the privatization, the appropriate federal agencies made the best decisions possible given the information we had at our disposal. We believed the decisions were the most judicious ones possible at the time and the most likely means of achieving the purposes of the statutes.

We believe that Congress provided a clear process for the government agencies to follow in accomplishing the privatization. The legislation set up a deliberation process that started with a Senate-confirmed board of directors outside of executive departments. The legislation also developed a rigorous process through which national security, labor, environmental, and post-closing conduct issues were collectively addressed by appropriate federal agencies. We believe Treasury and the other federal agencies involved in the process accomplished the objectives of the legislation in the most prudent manner possible at the time.

This concludes my written remarks. I will be happy to answer any questions you may have.

Mr. WHITFIELD. Okay. Mr. Moniz.

TESTIMONY OF ERNEST J. MONIZ

Mr. MONIZ. Mr. Chairman, thank you for the opportunity to present the Department of Energy's views on the issues before us today.

The Department has three core interests in the performance of a privatized USEC: Nonproliferation, particularly implementation of the HEU Agreement with Russia; security of supply, that is, the capability to secure or produce the enrichment requirements for meeting nuclear power industry and certain defense needs; and third, public policy commitments, particularly helping the gaseous diffusion plant work force and communities through a period of transition.

The administration and Department have been active in promoting these equities and I will spend a few minutes summarizing those actions. I will organize the remarks around two time periods following privatization, the relatively near term say the first 5 to 7 years, and the longer term beyond.

Let me start with the near term. At the time of privatization, a clear set of assets and responsibilities was transferred to USEC. These assets and responsibilities included, first, a robust market share of the domestic and international enrichment markets with significant long-term contracts in place at favorable SWU prices; a favorable lease arrangement for the Portsmouth and Paducah plants; favorable power rates for SWU production, thereby address-

ing the principal cost driver for the gaseous diffusion technology; transfer of significant uranium inventories with restrictions on entry into the U.S. market of approximately half of that inventory; HEU Agreement executive agency with a predictable cost of Russian LEU purchase negotiated by USEC and well below the market SWU price at the time of privatization; agreed restrictions designed to assist the work force and communities through the near term, including a cap on work force reductions and the requirement to operate both GDPs until January 2005 barring significant defined financial events; seventh, transfer advanced enrichment technology; and finally, virtually no liabilities from pre-privatization operations.

The private sector clearly viewed this balanced set of assets and opportunities and responsibilities favorably at the time of privatization, but the uranium-based markets have certainly proved to be weaker than was viewed then.

I would like to briefly describe some actions that we have taken in the last 20 months, but first let me emphasize that USEC has performed satisfactorily to this point as executive agent for the HEU Agreement. There has been much discussion over the last half year over whether the HEU Agreement responsibilities were an asset or liability for USEC. Perhaps the clearest indication of the HEU Agreement as a net asset to USEC is that USEC made the business decision on December 1, 1999, to continue as executive agent. If USEC had elected not to continue in that role, we were prepared—we had taken steps to identify alternative and/or additional agents interested in implementing the HEU Agreement from 2002 on.

A critical issue to the success of the HEU Agreement was resolution of the uranium feed issue about a year ago. I will just note that the administration played an important role in facilitating a solution to that problem. As part of it, of course, the Congress helped with appropriations allowing us to purchase 2 years' worth of uranium. We also pulled 22,000 metric tons of natural uranium off the market in the United States and, similarly, Russia is building up a comparable stockpile.

Currently, of course, a key issue is negotiation of the future pricing of the SWU component of the HEU contract between the U.S. and Russian executive agents for 2002 and beyond. The long-term market-based solution that we engineered for the feed component provides something of a template. And indeed the Russian Minister of Atomic Energy in meetings with the Secretary has explicitly acknowledged the need for a long-term agreement on market terms. The administration is actively supporting the negotiations and believes that market-based prices can and will be attained.

USEC's continuing strong order book and substantial cash-flow will help them sustain domestic enrichment capability for this period. However, a privatized USEC has also announced that further streamlining is required to maintain market competitiveness. The Secretary is strongly committed to assisting the GDP work force and communities through this period and will work closely with the congressional delegations, the unions, and others that represent these interests.

In addition to our work on the HEU Agreement in this context, several other actions have been taken. The administration has submitted a strong fiscal year 2001 budget request and an fiscal year 2000 supplemental request of $26 million designed to aid workers in the transition. The Department is consulting with the workers, the local community, and elected officials to determine the most appropriate means to minimize involuntary separations and the mix of separation benefits given available funds. The Department has provided about $14 million in local community assistance for developing employment opportunities. The Department is proceeding with plans to build and operate the DUF6 conversion facilities and plans to issue an RFP by October 2000 and award a contract in fiscal year 2001.

And finally, the administration is addressing significant environmental safety and health concerns at Paducah and Portsmouth. Just yesterday the Secretary, accompanied by key Members of this body, including Mr. Strickland, announced a major initiative to compensate workers made ill by exposure to radiation and toxic substances.

With the administration and congressional cooperation, we feel we can continue to balance public equities during this transition period.

But turning to the longer term, a key issue recognized very clearly prior to and at the time of privatization, is that a successor technology to gaseous diffusion—one that is less energy intensive and available for deployment in this decade—was needed. The June 1999 USEC business decision to discontinue AVLIS has clouded the path forward, at least temporarily.

USEC is actively addressing the alternatives, both centrifuge and laser-based technologies. The government has a continuing interest for both security of supply and workforce reasons. Steps taken include: a study on security of supply now ready for interagency review and requested by the Secretary immediately after the USEC AVLIS decision; the United States worked with the Australian government to facilitate cooperation on SILEX technology; and USEC has expressed an interest in evaluating centrifuge technology options and the Department, within appropriate bounds, is cooperating to provide technology access.

There is no doubt that heightened attention must be paid to long-term domestic enrichment capability in the aftermath of USEC's AVLIS decision. At the same time, implementation of a long-term market-based HEU Agreement will help provide stability in both the SWU and feed areas and we will continue multi-pronged support of programs that aid the workforce and communities by addressing health, remediation, and job creation issues.

Privatization of USEC reflects a long-standing bipartisan commitment by successive administrations and Congresses, as does the commitment to balancing the public interests of nonproliferation, security of supply, and community responsibility. We hope to continue that bipartisan commitment through the sometimes difficult period of transition. Thank you.

[The prepared statement of Ernest J. Moniz follows:]

PREPARED STATEMENT OF HON. ERNEST J. MONIZ, UNDER SECRETARY OF ENERGY

INTRODUCTION

Mr. Chairman, thank you for the opportunity to appear before your committee today and represent the Department of Energy in these deliberations concerning the United States Enrichment Corporation (USEC), its privatization and the domestic uranium industry.

I am Ernest Moniz. I have been Under Secretary at the Department of Energy since the end of 1997. Prior to that, I was Head of the Department of Physics at MIT and served as Associate Director for Science in the Office of Science and Technology Policy.

At the Department of Energy my areas of responsibility have been focused principally on the DOE's science and national security programs. My oversight in the latter area has included maintaining the nuclear stockpile and addressing nonproliferation challenges, particularly our cooperative programs to secure nuclear materials in Russia and to dispose of excess plutonium. As a result of the Department's work on a broad front with the Ministry of Atomic Energy of Russia, I have also been directly engaged in working to implement the US-Russian HEU Purchase Agreement. My work on integrating the DOE's R&D programs has included the issue of nuclear energy R&D for the future.

I will organize my brief remarks on USEC and the domestic uranium industry around several national level goals that reflect a Department of Energy perspective:

- *First, nonproliferation:* carrying out and sustaining the 1993 US-Russian HEU Purchase Agreement under which 500 metric tons of highly enriched uranium (HEU) are extracted from nuclear weapons in Russia and blended down, never to be used in weapons again.
- *Second, energy policy:* ensuring an adequate capability for securing or producing the enrichment and nuclear industry requirements of the United States.
- *Third, defense needs:* ensuring that we can meet defense needs that require domestic enriched uranium.
- *Fourth, public policy commitments:* supporting the equities embodied in the "Treasury Agreement" to our workers at the gaseous diffusion plants (GDPs).

These are not the only priority issues. But any path forward should address them.

The Energy Policy Act of 1992 created USEC to privatize the enrichment operations. The USEC Privatization Act of 1996 clarified many details of privatization and explicitly provided for the 1993 US-Russian HEU Purchase Agreement ("HEU Agreement") to supply uranium markets of the United States. Pursuant to such legislation, the President subsequently approved a privatization plan in 1997, and after conclusion of many complex agreements defining the terms of privatization, USEC became a private corporation in July 1998. Each step reflected a longstanding bipartisan commitment to privatization by successive Administrations and Congresses. The government's interests and role of USEC in various public policy issues and the uranium market are touched on below.

1. Nonproliferation and National Security

First, on national security, I will discuss the HEU Agreement, USEC's role in its implementation, and various challenges faced and overcome.

The end of the Cold War and collapse of the Soviet Union inevitably affected the world nuclear supply industry and uranium markets. Excess weapons material was destined to be sold into the world market. Such material contains much enrichment value (measured in separative work units, or SWUs) and uranium. The HEU Agreement provides an incentive for Russia to take material from nuclear warheads and blend them into low enriched uranium (LEU), instead of simply enriching more in their centrifuges and selling it on the world market, perhaps in a manner that lowers prices in the world market, as happened before the HEU Agreement.

The magnitude of the challenge in reversing the Cold War buildup of nuclear materials involves expenditures on the multi-billion-dollar scale. This inevitably leads to an intersection of governmental interests and the private sector, where the market for uranium based fuel involves revenues on the scale of billions of dollars. The HEU Agreement provides Russia incentives for continued dismantlement of weapons, and revenues that support Russia during a time of transition.

The HEU Agreement serves US national security interests, and is in Russia's interest as well. It is designed to take 500 metric tons of HEU (equivalent to about 20,000 weapons) from Russian weapons and blend it down for use and sale as commercial reactor fuel over twenty years. To date, the material derived from over 80 metric tons of HEU has been purchased and sold, ridding the equivalent of more than 3,000 nuclear weapons. The HEU Agreement is a government to government

agreement that defines a framework that is implemented through commercial means.

USEC is the current US executive agent, having signed an implementing contract with Russia's executive agent in 1994, and begun payments to Russia in 1995 for deliveries that have continued yearly since then. USEC has performed satisfactorily under an agreement that defines USEC's role as executive agent. The US can replace or add an additional agent, just as USEC can give notice that it no longer desires to serve as such.

It should be noted that there are essentially two tracks in implementing the HEU Agreement, as it has evolved. *First,* the portion USEC pays Russia for the SWUs, which is about two thirds of the value of what Russia physically delivers to USEC. USEC uses the Russian delivery to provide enriched uranium to its utility customers. *Second,* Russia, for every delivery to USEC, is by US law awarded title to an amount of natural uranium that is contained in the enriched uranium purchased by USEC. Russia then seeks to realize the remaining value of the HEU Agreement through natural uranium sales, in the US under the schedule limits set out in the Privatization Act of 1996, or internationally.

The natural uranium track (or "feed component", as it is sometimes called) complicated implementation of the entire HEU Agreement on several occasions starting in early1997. Russia's export guidelines in the past stopped deliveries to USEC, because of the lack of payment and a path forward on payment for its natural uranium. An agreement signed by Secretary of Energy Richardson with his Russian counterpart early last year solved this problem. This "HEU Feed Transfer Agreement" ("Transfer Agreement") used $325 million appropriated by the Congress for DOE to purchase the 11,000 metric tons of unsold Russian natural uranium that had accumulated in the United States, added it to an existing 11,000 metric ton DOE stockpile, provided for holding this total off the market for 10 years, and defined a long term commercial path forward for the feed component for the duration of the HEU Agreement.

The DOE through the Transfer Agreement, and in the interest of the market, thus pulled 22,000 metric tons (nearly 60 million pounds) of natural uranium off the market for a decade, uranium that was otherwise slated to be sold over this period and the future proceeds for which will go to the Treasury. In addition, what Russia does not sell to a western consortium of companies pursuant to the annual quotas in the 1996 US law, will be returned to a Russian stockpile where, until it reaches a 22,000 metric ton amount, can only be sold into long term contracts with the consortium, or used to blend down more HEU from Russian weapons. To date, because of the current market, most of the Russian feed is slated for transport back to Russia's stockpile, and thus will not soon come into the US market.

More recently, issues have arisen in implementing the HEU Agreement that directly involve USEC. One involves the question whether the SWU portion of the HEU Agreement is a liability or an asset to USEC, and if so, what the government should do. Another is the pricing of SWU from Russia for the balance of the HEU Agreement.

Public statements by USEC prior to privatization suggested that USEC viewed the Russian supply of SWU as a strategic asset, particularly after USEC negotiated a pricing mechanism with Russia that went into effect in 1997 and extends through 2001 deliveries. Indeed, this pricing mechanism reflected a discount off the spot market price at the time of the signing of the contract amendment, escalated by an agreed inflation metric. The low enriched uranium (LEU) supplied by Russia under the HEU Agreement and its pricing was therefore part of a known mosaic of assets (e.g., favorable electricity rates for SWU production, sales contracts, transfers of uranium inventories, Russian LEU at a price negotiated by USEC) and responsibilities that transferred to the privatized USEC. The US government did not rule out in the latter part of 1999 examining what, if anything, might be appropriate under changed conditions, particularly in the full context of other public equities to be discussed below. But based on our assessments, we are not persuaded that the HEU Agreement was a net liability, compared to USEC's ability to produce and replace the enrichment services from Russia.

In certain respects, the issue was put to the test on December 1, 1999. USEC made a business decision to continue as executive agent with certain legal obligations to perform through 2001. The US also took steps to identify other alternative or additional agents interested in implementing the HEU Agreement.

The US endorses USEC's efforts to reach agreement on commercial terms with Russia's executive agent on a pricing mechanism for SWU to succeed the current mechanism that applies through 2001. Indeed, Russia acknowledges a continuing need for market based contracts, as in the agreement on HEU feed. Both the Russian and US governments are monitoring these discussions, mindful of the interests

of their agents, as well as broader equities. A stable commercial mechanism for the SWU that complements the long-term commercial agreement for the feed component is desirable.

2. Security of Supply and Enrichment

Second, I will discuss the impact of the HEU Agreement on the US, and related issues on security of supply and enrichment of uranium for the United States, as they have evolved since 1998.

The uranium imported into the US as a result of the HEU Agreement affects the US market (as would the absence of such an agreement). This is more evident now that the HEU Agreement has proceeded from an initial annual purchase of 6 metric tons in 1995 to an annual 30 metric ton annual amount in 1999 and for the duration of the agreement to 2013. In addition, various nuclear plant closures over this period have also impacted world demand. An annual report provided to the Congress reflects the impacts of implementing the HEU Agreement, in conjunction with other developments.

The HEU Agreement is slated to provide from 1999 onward 5.5 million SWU per year which represents somewhat less than half of USEC sales in recent years when combined with their production at the gaseous diffusion plants in Ohio and Kentucky. DOE leases these plants to USEC. USEC may not close one of these plants until January 2005 because of its obligation to continue operating the plants until that time, absent a significant financial event.

The US government, therefore, for reasons of national security and energy policy needs to ensure that the balance of interests is maintained in regard to security of supply in the coming years. There are several noteworthy points in this regard:

- One, the HEU Agreement has over time become an important source of supply for enrichment for the U.S. nuclear industry. Given the availability of nuclear material for such purposes, the benefits of this commerce outweigh, in general terms, the risks on the supply side.
- Two, USEC's decision in June 1999 to discontinue the Atomic Vapor Laser Isotope Separation (AVLIS) enrichment technology clouds the path forward for a replacement technology for the GDPs, particularly one that is less energy intensive and available in the desired time frame. Secretary Richardson asked for a study of the consequences of this decision for US energy security immediately after USEC's decision. The Department has completed this study and, at the direction of the Enrichment Oversight Committee, it is ready for review by other agencies. USEC, meanwhile, is reviewing other possible enrichment technologies, such as centrifuges and laser-based approaches. The Department is, as appropriate, aiding USEC's evaluation of certain enrichment technologies.
- Three, the evaluation of USEC's credit rating this year has raised concerns about USEC plans for the GDP's over the next several years as they evaluate long term replacement technologies.

Until last year, on the basis of the combination of factors such as favorable power contracts through 2005, low costs of leasing the GDPs from the Department, and ongoing R&D on AVLIS, a path forward on future domestic enrichment capability was clearer. In the aftermath of USEC's decision in 1999 on AVLIS, however, the Secretary immediately focused on what the long-term implications would be. USEC is pursuing its R&D on the SILEX enrichment technology, and the US worked with the Government of Australia to enable this cooperation funded by USEC to proceed. Meanwhile, more recently, USEC has expressed interest in evaluating centrifuge technology options, and the Department has cooperated to that end, within appropriate bounds. The study on security of supply initiated last year by the Secretary is part of the heightened attention that must be paid to long-term domestic enrichment capability following the USEC cancellation of AVLIS development.

3. Defense Needs

Third, I will note briefly specialized but important defense needs that pertain to domestic enrichment capacity and uranium inventory management, as well as some potentially beneficial market consequences that may result.

In late 1998, the US decided to produce its future tritium needed for the stockpile in Tennessee Valley Authority (TVA) light water reactors. To comply with various nonproliferation commitments it is important to ensure that the uranium and enrichment are of US origin in the reactors producing tritium. The TVA and USEC last year signed an enrichment services contract that some uranium analysts believe may cover some 15-20 million pounds of natural uranium for the 10-year contract. Thus, USEC planning for the TVA contract may address some concerns over the disposition of its uranium inventory in the market.

In addition, the Department monitors the long-term enriched uranium needs of its naval reactors program.

4. Public Policy Commitments

Fourth, I want to return to public policy commitments to workers at the GDPs that I noted above in a different context of security of supply. Secretary Richardson feels very strongly about these issues.

I noted earlier the Treasury Agreement that USEC signed shortly before privatization. The working premise of the agreement is that both enrichment plants, leased by DOE, to USEC would be kept open through 2004 and work force reductions were capped until June 2000. For the Secretary's part, any prospect of federal support that had not been contemplated prior to privatization certainly should not be considered now if it did not reinforce previous commitments made to the federal government and to GDP workers. Indeed, any other approach would put the government in the position of appearing to benefit private sector parties while ignoring or harming existing federal commitments.

I know you are aware of recent reports regarding significant environmental, health and safety concerns at the gaseous diffusion plants. As part of our response to these developments, the Department has developed initiatives for additional funding in fiscal year 2001 to accelerate cleanup and protect health and safety at the GDPs in Ohio and Kentucky. Such initiatives include remedial actions to dispose of low-level waste and clean up old landfills, oversight investigation of past and current practices, reviewing uranium flows to assess potential worker exposures, establishing worker radiation exposure profiles, and expanding medical surveillance for current and former workers.

The Administration has a proposed an initiative to compensate workers made ill by exposure to radiation and toxic substances while working to build America's nuclear defense. The levels of compensation for federal and contractor workers at the three GDPs in Kentucky, Ohio and Tennessee formerly run by DOE, are similar to those established in the initial compensation legislation proposal submitted to Congress in November 1999.

The Administration has also submitted a $26 million fiscal year 2000 Supplemental Budget Request to the Congress to address additional concerns, including $10 million for Environmental, Safety and Health activities (health studies, oversight), and $16 million for environmental restoration. The Department urges the Congress to act on these requests as soon as possible.

USEC earlier this year announced some 850 layoffs at the GDPs to occur this summer that were long anticipated. The FY 2001 budget and the supplemental request for the Environmental Management program support the Secretary's efforts to aid workers in the transition.

The Department is consulting with workers, the local community, and elected officials to determine the most appropriate means to minimize involuntary separations and the mix of separation benefits for workers who do not transition that can be supported with available funds. The Department has provided $13.8 million in assistance to local communities for activities that can provide employment opportunities for displaced workers and additional community assistance requests are currently under review.

In addition, the Department is proceeding with plans for a project to build and operate conversion facilities to chemically convert depleted uranium hexafloride inventories into a form better suited to both storage and ultimate disposition. This has been paced principally by characterization of contamination in the depleted uranium inventory, sampling analysis of which should enable an RFP to be issued by October of this year, award of contract in fiscal year 2001, and the initiation of design.

Concluding Remarks

I have set out some of the basic governmental interests from DOE's perspective in:

- Performance on the HEU Agreement;
- Monitoring security of supply of enrichment, relative to private sector plans, market availability and national reserves;
- Meeting defense needs; and
- Fulfilling public policy equities to GDP workers.

I have noted, where appropriate, USEC's role, or uranium market impacts of the HEU Agreement or governmental actions.

In closing, I note that the end of the Cold War has posed novel challenges and opportunities.

The impetus to create USEC came out of the 1980s and was to privatize enrichment in a bipolar world. It would have been hard to imagine in the mid-1980s dur-

ing a build up of nuclear weapons that, little more than a decade latter, concerns would be raised about the rate at which material from dismantled Russian nuclear weapons comes into the US, or that questions would arise about sustaining US enrichment capability or what future options are best.

In the post Cold War context, it has always been understood that a private executive agent implementing the HEU Agreement with Russia could experience tensions between its commercial interests and the government's immediate preferences. This is a perpetual tension to be managed. In the end, the government will have its interests served, or take corrective steps. However, the complex intersection of governmental and private interests is a fact of life driven by the large scale of resources needed to reverse Cold War buildups (HEU, plutonium, weapons complex). Much has been accomplished, and given the scale of the problems created over many years, much remains to be done.

We need the support of the Congress on all these issues and look forward to working with you. I would be pleased to respond to any questions you may have. Thank you.

Mr. WHITFIELD. Thank you.

Mr. Paperiello.

TESTIMONY OF CARL J. PAPERIELLO

Mr. PAPERIELLO. Mr. Chairman, it is my pleasure to appear before you today to discuss the U.S. NRC's financial review of the USEC. Under the USEC Privatization Act of 1996, the NRC is required to determine if the issuance of a certificate of compliance would be inimicable to the maintenance of a reliable and economic domestic source of enrichment services. In February of this year the NRC initiated a review of USEC's financial condition because NRC's basis for its previous determination had changed, when on February 4, Standard & Poors downgraded USEC's corporate credit rating to below investment grade.

I'd like to clarify something that I heard today. The NRC used the corporate credit rating for the initial public offering path. And we had developed a standard review plan to deal with either path, a sale of the company or an IPO. The decision to use the credit rating was based upon extensive conversations with both financial managers in the private sector as well as Federal agencies, including the U.S. Treasury and the Securities and Exchange Commission.

When the NRC recertified USEC's operation of the gaseous diffusion plants in January 1999, USEC had investment grade credit ratings from both Moody's investors service and Standard & Poors. On February 3 of this year, USEC announced lower financial projections for fiscal 2001, a plan to lay off 850 employees, a dividend rate cut to half its previous value, and a program to repurchase stock. On the next day, Standard & Poors reacted to this announcement by downgrading USEC's credit rating from BBB to BB+, a below investment grade rating. And on February 23, Moody's downgraded USEC from Baa1 to Ba1, also below investment grade rating.

As I note, recertification was based in part on USEC's investment credit ratings. Consequently, we have reopened the financial review of USEC to evaluate changed conditions. And this review of the financial status is consistent with typical agency practice whenever the basis for issuing a license, in this case a certificate for operating the gaseous diffusion plants—when that changes we will then turn around and reinvestigate the basis for our licensing decision.

We are evaluating the projected financial condition of USEC anticipated for the next 5-year period consistent with the guidance that we have published in our standard review plan for recertification of the gaseous diffusion plants. I should point out that when we wrote the initial standard review plan for the initial certification, it was a public document. We shared it with everybody. The uranium—the Enrichment Oversight Committee saw it, so it was not something that we did in a vacuum.

And, of course, since they have dropped below investment grade, additional analysis will have to be done. We will be using consultants. We don't have that many people on our own staff who are qualified to look into business plans, projected financial statements, and other financial information. We plan on providing our analysis and recommendation to the Commission in early summer of this year. And any Commission recommendations, as appropriate, would be forwarded to Congress and the Enrichment Oversight Committee.

I also have to note that the NRC staff's major efforts at the gaseous diffusion plants remain the protection of the workers' and public's health and safety, protection of the environment, and the assurance of the common defense and security of the United States.

In conclusion, we have reopened our financial evaluation of USEC following the recent corporate credit rating downgrades from Moody's and Standard & Poors, and based on a staff evaluation the Commission will forward any appropriate recommendations to Congress and the Enrichment Oversight Committee for use in making future decisions regarding domestic enrichment service.

This is concludes my oral statement.

[The prepared statement of Carl J. Paperiello follows:]

PREPARED STATEMENT CARL J. PAPERIELLO, DEPUTY EXECUTIVE DIRECTOR FOR MATERIALS, RESEARCH, AND STATE PROGRAMS, U.S. NUCLEAR REGULATORY COMMISSION

Mr. Chairman and Members of the Subcommittee: It is a pleasure to appear before you today to discuss the U.S. Nuclear Regulatory Commission's (NRC's) financial review of the U.S. Enrichment Corporation (USEC) and the status of several important regulatory activities. Under the USEC Privatization Act of 1996 (P.L. 104-134), the NRC is required to determine if the issuance of a certificate would be inimical to the maintenance of a reliable and economical domestic source of enrichment services. In February of this year, NRC initiated a review of USEC's financial condition because NRC's basis for its previous determination had changed when, on February 4, 2000, Standard & Poor's (S&P) downgraded USEC's corporate credit rating to below investment grade.

When NRC recertified USEC's operation of the gaseous diffusion plants in January 1999, USEC had investment-grade credit ratings from both Moody's Investors Service (Moody's) and S&P. On February 3, 2000, USEC announced lower financial projections for fiscal year 2001, a plan to lay off 850 employees, a dividend rate cut to half of its previous value, and a program to repurchase stock. On February 4, 2000, S&P reacted to this announcement by downgrading USEC's credit rating from BBB to BB+, a speculative rating. On February 23, 2000, Moody's downgraded USEC from Baa1 to Ba1, also a speculative-grade rating.

NRC's recertification of USEC in early 1999, in part, was based on USEC's investment-grade credit ratings. Consequently, NRC re-opened the financial review of USEC to evaluate the changed conditions in light of the changes that occurred in the financial market in February. Reviewing the financial status is consistent with typical agency practice if the basis for authorizing an activity, such as operating the gaseous diffusion plants, changes anytime after the authorization. We believe this is consistent with the authority Congress provided to the NRC in the USEC Privatization Act of 1996.

NRC staff is evaluating the projected financial condition of USEC anticipated for the next five-year period consistent with the NRC guidance developed specifically for USEC. This review examines business plans, projected financial statements, and other information applicable to the critical issues affecting USEC. On February 25, 2000, NRC requested USEC to provide the information to support this review by the end of March. Last month, USEC requested some additional time to assemble and submit the information.

To guide such certification reviews required in 10 CFR Part 76, NRC staff developed a "Standard Review Plan for Recertification of the Gaseous Diffusion Plants," NUREG-1671 (SRP), last updated in February 1999. The section of the SRP describing the financial review was approved by the Commission in November 1997 to include the privatization effort. Chapter 16 of the SRP describes the procedures and criteria for conducting these reviews to implement the requirement in 10 CFR 76.22(b)(2), which states "A certificate of compliance may not be issued to [USEC] if the Commission determines that . . . the issuance of such a certificate of compliance would be inimical to . . . the maintenance of a reliable and economical domestic source of enrichment services." The NRC established this requirement to implement section 193(f) of the Atomic Energy Act, et. seq. (42 USC 2243). The SRP includes an examination of the credit strength and financial condition based on credit ratings from rating services such as Moody's and S&P. During the transfer of the certificate to the privatized corporation in July 1998, consistent with the SRP, NRC determined that USEC had a financial structure that included an investment-grade rating from Moody's or S&P and, therefore, met the long-term economic viability requirements. Under the SRP, a speculative rating could also be acceptable, but additional criteria and an analysis would be required.

NRC staff plans to provide its analysis and recommendations to the Commission in early Summer 2000. Any Commission recommendations, as appropriate, would be forwarded to Congress and the Enrichment Oversight Committee, a group of representatives from several Executive Branch agencies including the Departments of Treasury, Commerce, Energy, and Defense, the Office of Management and Budget, and the National Security Council. Any recommendations could then be used by Congress and the Executive Branch to determine the need for any future government actions.

The NRC staff is also working on several other important regulatory activities associated with the gaseous diffusion plants, including the Paducah seismic modification project, the Paducah enrichment upgrade project, a review of USEC's safety program, and continued oversight to ensure that layoffs at Paducah and Portsmouth do not adversely impact safety and safeguards at either plant. DOE identified in 1995 the vulnerability to earthquakes of two of the process buildings at Paducah. NRC incorporated requirements to strengthen building structures in the Compliance Plan when the plant was certified in 1997. The Compliance Plan is an NRC-approved plan requiring USEC to achieve compliance with regulatory standards on a set schedule. Since that time there have been several program delays in the seismic upgrades due to the identification of several unreviewed safety questions, unexpected construction difficulties, and characterization by the DOE of its Material Storage Areas, where some of the seismic construction work is taking place. DOE and USEC reached agreement on an approach in early February 2000, which allows characterization of the DMSAs by July 2000 and completion of the seismic upgrades by September 2000. Since that time, USEC has continued to make progress on both programs.

In 1999, USEC announced its intent to increase the enrichment level of uranium processed at Paducah. The Paducah Higher Assay Upgrade Project would increase the maximum product enrichment from 2.75 weight percent to 5.0 weight percent uranium-235 (U-235). Because 5 weight percent enriched uranium cannot be used for military applications, there are no national security issues from this upgrade. The increase in enrichments must be authorized by USEC requesting and NRC amending the certificate for Paducah. NRC approval of the enrichment amendment request depends on a number of factors, including the technical adequacy of several licensing submittals that USEC plans to submit between now and September. The NRC expects to review the submittals during the remainder of this year and into early 2001.

The third significant regulatory activity for both Paducah and Portsmouth involves confirmation of the adequacy of the safety programs to protect workers, the public, and the environment. In response to public and Congressional concerns about worker protection and historical exposures as a result of processing and handling reprocessed reactor fuel material from the 1950s to the mid-1970s at Paducah and Portsmouth the NRC conducted special confirmatory inspections in September and October of 1999 of USEC's radiation safety programs. Following the inspections,

the NRC held public exit meetings near the Paducah and Portsmouth sites. NRC's inspections concluded that USEC's radiation protection programs at both sites were adequate and met NRC requirements. The inspections also confirmed that the environmental releases of radioactive materials from USEC's operations were well within NRC limits and that the environmental monitoring programs were adequate. However, the inspections identified that some of the workers were not aware of certain radiological hazards or radiation protection requirements and that the radiation protection training did not include site-specific information regarding radiological hazards from transuranic radionuclides. In addition, at Paducah, the NRC concluded that certain unsupported assumptions were being made in calculating internal doses because they did not adequately include a contribution from some transuranic radionuclides. Although the inspection confirmed that the sites' airborne radioactivity levels and, thus, worker and public risks were low, the NRC concluded that USEC's assumption that there was no contribution from some transuranic radionuclides was not supported by recent measurements. Since the inspections, USEC has taken actions to strengthen its radiation protection programs. The NRC staff continues to review USEC's corrective actions as part of its ongoing inspections.

NRC has also been conducting similar licensing reviews to confirm the adequacy of each site's nuclear criticality safety program to protect against the risk of a nuclear criticality accident. USEC is required by regulation to demonstrate the adequacy of its nuclear criticality safety program in preventing a criticality accident in plant areas where it judges that there is a potential for criticality accidents. The staff has several review actions under way in an attempt to confirm the adequacy of each criticality program and to require USEC to correct or mitigate any significant deficiencies.

The final activity that I would like to discuss briefly is NRC's continuing review of USEC's performance in the transition phase leading up to and following any layoffs. There are regulatory requirements for minimum staffing levels and overtime usage, and reduced staffing can affect critical functions such as plant operations and maintenance. There are two resident inspectors at each gaseous diffusion plant, who regularly observe daily plant operations and interface with the plant staff. The resident inspections are supplemented with specialist inspections in such areas as radiation protection, fire protection, nuclear criticality safety, chemical process safety, and material control and accounting. To ensure that continued staffing changes do not detract from the protection of public health and safety and safeguards at the plants, NRC staff has increased its regulatory oversight during the transition phase. In addition, NRC will conduct increased safety and safeguards inspections, conduct meetings with USEC management, the public, and other stakeholders on the transition activities, and monitor performance trends such as backlogs, operational events, overtime usage, and compliance with regulatory commitments.

In conclusion, we have re-opened our financial evaluation of USEC following the recent corporate credit rating downgrades from Moody's and S&P. Based on the staff evaluation, the Commission will forward any appropriate recommendations to Congress and the Enrichment Oversight Committee for use in making future decisions regarding domestic enrichment services. The NRC staff is also continuing to monitor closely USEC's performance at the plants to ensure protection of public health and safety and safeguards.

Thank you, Mr. Chairman. I would be pleased to answer any questions that you and Members of the Subcommittee may have.

Mr. WHITFIELD. Mr. Paperiello thank you very much and thank all of you for your testimony.

Mr. Paperiello, let me ask you a couple of questions. Since USEC has been privatized, how many times has the NRC fined USEC for unsafe operations?

Mr. PAPERIELLO. In the past year, year and a half, I'm aware of two occasions. There might have been some earlier. I just don't have the number—I could find it out, but I just don't know.

Mr. WHITFIELD. Were there civil fines associated with that?

Mr. PAPERIELLO. Yes, in the past year, maybe 15 months, we have issued a fine to Portsmouth as a consequence of a fire that occurred in December 1998. And we recently issued a fine to Paducah for employment discrimination.

Mr. WHITFIELD. And do you know about what the dollar figure was?

Mr. PAPERIELLO. The second one was, I believe, $88,000. I think the one at Portsmouth was $50,000 in that range, but I know I'm under oath. It is in that order.

Mr. WHITFIELD. The NRC is now considering an application of USEC to enrich uranium up to 5 percent or 5.5 percent at the Paducah plant. And allegations have been made by certain employees there, as well as others, that in the criticality safety area that NRC is applying a different standard in this evaluation than they have in the past. What is your comment about that?

Mr. PAPERIELLO. Yes, they have a program to upgrade the enrichment percentage at Paducah. It is a program—as explained to us, will require them to submit, I think, as many as five license or certificate amendments.

The first amendment came in, I think, at the end of last year and somewhere in the February timeframe. We rejected that application. It was an application to change the limit on enrichment at certain portions of the plant. We rejected it because they did not provide an adequate technical basis. As you're aware, criticality is potentially a very serious problem at any fuel facility. We all know what happened in Japan last year. And there was not an adequate technical basis—that was the basis of our rejection. It had nothing to do with change in policy, at least from our viewpoint, but it was an increase in the enrichment over what the facility—at those stations that had been originally designed for without an adequate technical basis.

Mr. WHITFIELD. And when do you expect a decision would be made upon this application?

Mr. PAPERIELLO. We don't have applications in front of us. They laid out a timeframe to us for when they would be submitting information. You made reference to a letter that we sent them. I don't know if it is the letter I read, but the letter I read, we basically said we are not going to be able to do this by the end of this calendar year if some of the information you're going to submit to us isn't going to come in until November. That was the point.

Mr. WHITFIELD. Okay. And so you don't have all the information at this point.

Mr. PAPERIELLO. We do not have all the information. What we were replying to was the timeframe that they were laying out to us.

Mr. WHITFIELD. Mr. Moniz, at privatization, a large sum of uranium was transferred to USEC as a part of that privatization agreement. Did you have any concern that their selling it on the open market would possibly drive down the price of uranium?

Mr. MONIZ. First, I should note there was a large transfer of uranium consistent with the EPACT requirements and then a second transfer——

Mr. WHITFIELD. Was the first transfer 30 million pounds?

Mr. MONIZ. No, that was approximately 120 million pounds, I believe. However, of that only 23 million pounds was DOE-owned uranium.

Mr. WHITFIELD. And what was the second one?

Mr. MONIZ. I could get that for you later on. Quite a bit of the first transfer, more than 90 million pounds was actually owned by utilities. The second part—thank you, here it is. The total EPACT transfers were about 140 million pounds, and the Privatization Act transfers 31 million pounds.

Also I will note that we have taken, as I mentioned in my oral statement, we have actually taken 58 million pounds of DOE uranium off the market for 10 years which compensates for part of that. In the transfer, more than half of the uranium had restrictions on its entry into the market. We—the Secretary wrote to the corporation, in fact, late last year, asking questions about this, and the corporation has responded in terms of their plans to market at the rate of 10 percent of worldwide market demand.

Mr. WHITFIELD. Mr. Mark Stout of the Uranium Producers of America will be testifying later today and in his testimony he says that USEC's selling of this uranium on the market is decimating their industry. Do you have any reaction to that?

Mr. MONIZ. Well, it's clear the market is soft, prices have fallen substantially. I think the USEC sales certainly contribute to it, although we believe they are not the only element. There have been significant liquidations of supplies, for example, by various groups.

Mr. WHITFIELD. I have one more question and then we will proceed.

Mr. Gensler, Mr. Stiglitz was chairman of the President's Council of Economic Advisors and was serving in that capacity when discussions were being considered in the administration about whether or not USEC should be privatized. And he was very strong in his view that it should not be privatized, and he enumerated certain reasons that have come to pass. In your involvement with the discussions on the decision to privatize or not privatize, were there other people in the administration that were as opposed to it as Mr. Stiglitz, from your recollection?

Mr. GENSLER. Just for the record, I actually joined the administration after, I think, Mr. Stiglitz went on to his important duties at the World Bank, so I don't know in a comparative sense. But I am aware of his points of view and that as we move forward, we looked at this in a thorough way with regard to the statutory criteria. And having had that debate before the President—before the 1997 opinion to move forward, which actually was before I joined the administration.

Mr. WHITFIELD. Mr. Stupak.

Mr. STUPAK. Thank you, Mr. Chairman. Mr. Moniz, I thought you just said in your testimony that dumping on the market was not driving down the price of the U.S. SWUs; correct?

Mr. MONIZ. The discussion we just had of natural uranium? And I said certainly sales in fact by anyone, and certainly by USEC, added to the current market condition. What I added was that there were other sources as well of uranium that lowered the market price.

Mr. STUPAK. Okay. There was a document that was just handed in front of you and it is part of the record. Right there by your name plate there. If you could take a look at it. It goes—it states: As a result, USEC has been selling natural uranium stocks re-

ceived through privatization and conversion services to raise cash to sustain itself.

This is about the third paragraph, last line.

Natural uranium prices have as a result fallen to new lows despite the March 1999 U.S.-Russian Transfer Agreement intended to shore up the natural uranium tract of the HEU Agreement.

Is that an accurate statement?

Mr. MONIZ. Yes, again I would just add it is not the only driver of the prices.

Mr. STUPAK. Let's read on here a little bit. It says the Russians feel like they don't have to reduce their returns to benefit USEC stockholders, so it wouldn't give USEC a lower price on SWUs this year. Is that also correct?

Mr. MONIZ. I cannot confirm the Russian attitude. This was an analysis done.

Mr. STUPAK. That's what it says in the next paragraph there; right?

Mr. MONIZ. Yes, but this was one person's analysis.

Mr. STUPAK. DOE analysis.

Mr. MONIZ. Correct. All I'm saying is I don't know if it correctly reflects the Russian view.

Mr. STUPAK. Or DOE is not correct?

Mr. MONIZ. It could be. This is an analysis.

Mr. STUPAK. Okay. Let's get down to the bottom line of USEC's bailout proposal as DOE saw it. The USEC wanted $200 million or USEC would withdraw as the executive agent under the HEU plant and—quoting now—in addition, USEC might choose to close the Portsmouth, Ohio, plant in the near term. This would save the company approximately $113 million per year, but would cause unemployment for 1,500 people that were provided some assurances or reassurance in a 1998 Treasury agreement that they would be employed through 2004.

So either USEC gets $200 million, or 1,500 people are out of work and the government has no executive agent. That basically was the proposal and that's the way it was analyzed there; right?

Mr. MONIZ. That was one analysis presented. You are certainly correct that at that time, people——

Mr. STUPAK. That is one analysis by DOE; right?

Mr. MONIZ. Correct.

Mr. STUPAK. That sounds a bit like blackmail, doesn't it? Either you give us $200 million or we close down this plant and 1,500 people are unemployed.

Mr. MONIZ. USEC made an argument in terms of statements about spot market prices versus HEU Agreement prices and from that calculated $200 million.

Mr. STUPAK. Or 1,500 people are laid off.

Mr. MONIZ. Sir, I am certainly not aware—I am personally not aware of that statement ever having been made.

Mr. STUPAK. But you cannot close a plant before 2005 unless there is a significant event; right? Is that the agreement?

Mr. MONIZ. Correct. That is part of the Treasury agreement; yes, sir.

Mr. STUPAK. And now we get this proposal or analysis that was made—and I guess it was made at the White House—dated No-

vember 12, 1999, stating that the bailout would protect, "continued plant operations that otherwise would be in jeopardy in Ohio and Kentucky." What would be a significant event which would lead to the closure if you have assurance it is going to be open until 2005?

Mr. MONIZ. Actually, Mr. Gensler may want to answer that. There are a set of conditions spelled out in the Treasury agreement as to what would constitute such a significant event. They are well-defined financial benchmarks.

Mr. STUPAK. Okay.

Mr. GENSLER. The concept was that which might go to the viability of the organization. And they were reductions of earnings to certain levels, reductions of SWU pricing to certain levels or operating margins, and as we have talked about here——

Mr. STUPAK. Have any of these significant events occurred yet?

Mr. GENSLER. As I said in my prepared remarks, we informed USEC in January that if they thought there was a significant event, they should so notify us. They haven't notified.

Mr. STUPAK. They have noticed you of any significant event?

Mr. GENSLER. They have not done so.

Mr. STUPAK. Is their credit rating below what it should be, the investment credit?

Mr. WHITFIELD. Mr. Stupak, if you would finish up this question, then we will move on to Mr. Strickland.

Mr. STUPAK. Oh, I'm sorry.

Mr. GENSLER. I think if the question is—let me just state factually as I understand it, that in early February, as noted earlier by one of my administration colleagues, was downgraded by Moody's and S&P. Each of those downgrades, as was currently stated on the record, are noninvestment great.

Mr. STUPAK. So in your agreement that is a significant event?

Mr. GENSLER. Again, we have not been notified as such by USEC, and we think it is really, as we said in January, incumbent upon them to come to us and tell us their thinking if they are so considering such an action.

Mr. STUPAK. That is one of the events in that agreement. Right? That's one of the significant events in the agreement, yes or no?

Mr. GENSLER. The agreement does list noninvestment grade rating as you so suggest.

Mr. STUPAK. Thank you.

Mr. WHITFIELD. Mr. Strickland.

Mr. STRICKLAND. Mr. Gensler, is there anything in the Treasury agreement that requires USEC to notify Treasury that a significant event has occurred?

Mr. GENSLER. We believe that they do have that obligation. We so put them on notice in January with regard to that.

Mr. STRICKLAND. If they have got that obligation and one of the conditions had been met, then who has got the responsibility for pursuing this? Under the terms of the agreement, who has an obligation to determine a significant event has occurred?

Mr. GENSLER. The terms of the agreement are that they have an obligation to keep those plants, both plants open till——

Mr. STRICKLAND. How do they inform you of that?

Mr. GENSLER. I think there are many ways they can inform us. They haven't sought any of those ways——

Mr. STRICKLAND. Then are we assuming that USEC——

Mr. GENSLER. [continuing] ways to inform us if they were so considering taking it to their board.

Mr. STRICKLAND. Then can we assume—and as the Treasury Department, I think you have an obligation here. Can we assume that USEC is not meeting their obligation to inform you that a significant event has occurred if a significant event has occurred and we all know it has? Come on, we can read.

Mr. GENSLER. I actually have to say there are two components of it. Whether they are considering and taking to their board such dramatic action that I know this committee, we are all very interested in, and the question of significant event. They have not informed us of either of those.

Mr. STRICKLAND. If they inform you that such an event has occurred, will you commit to us that you will investigate whether or not Morgan Stanley's recommendation was followed by USEC's management in manipulating circumstances so that such an event would occur?

Mr. GENSLER. I would say that if such time comes that they inform us, that we will look at all relevant factors at that point in time. To your earlier question, sir, as I recall from the earlier panel, I would say that I think it would be quite a risky path for any company to take, but particularly this company and quite an unusual a path to take to try to——

Mr. STRICKLAND. Don't you think it is interesting that Morgan Stanley would put in writing such a recommendation? I assume that would be unusual for a company like Morgan Stanley as well, but they obviously have. I don't think it would be unusual for us to presume that USEC may have taken advice from Morgan Stanley since Morgan Stanley was intricately involved in advising over the entire privatization process having received multiple, multiple, multiple millions of dollars; and Morgan Stanley has been very public in saying they think that USEC needs to close one of the two plants. It seems to me there is a relationship, some relationship between USEC and Morgan Stanley.

I have a series of questions that I think you could answer yes or no. Were you aware that administration officials, including Dr. Stiglitz, opposed privatization based on national security concerns? Just a yes or no answer if you would.

Mr. GENSLER. I was aware of that.

Mr. STRICKLAND. Were you aware of concerns raised by Senator Domenici in this letter to Secretary Burger raising concerns about national security matters regarding privatization?

Mr. GENSLER. I was aware, and I know that the national security part of the administration did a thorough review of those matters.

Mr. STRICKLAND. Did it surprise you that USEC showed up last fall asking for a $200 million bailout or threatening to possibly walk away from the executive agent status?

Mr. GENSLER. I would say that I was very encouraged that on December 1—they stayed with that status—that they tried to negotiate or bring to Congress their private sector concerns. I think we are fortunate that they stayed with that agreement even though Congress saw fit to move forward without giving them that money.

Mr. STRICKLAND. Were you responsible as a senior official of the administration for advising the USEC board on national security issues before privatization?

Mr. GENSLER. No, I was not.

Mr. STRICKLAND. I have a copy of a transcript here in which Chairman Rainer—this was immediately before privatization—in reaction to questions raised by Mr. Burton, who was one of the board members, regarding being briefed by the NSC in regard to the matters raised by Senator Domenici and others and I quote from Mr. Rainer in response to Mr. Burton, "I gave you some information saying that I talked to Gensler and they are prepared to move ahead. Can't you derive answers from that? Don't you have the ability to derive answers from the fact that Gary Gensler said senior people in the administration had been all over this thing for days and days and days and we should take confidence in the fact that they are expecting us to move ahead with privatization?"

Was Mr. Rainer inaccurate in describing his conversation with you regarding these national security matters?

Mr. GENSLER. With all respect, I am not sure what the context of that conversation was in the meeting that you are referring to.

Mr. STRICKLAND. Well, Mr. Burton was raising questions and Mr. Burton was asking that before privatization the board be briefed on these national security matters, and his request for such a briefing was denied. Does this seem improper to you that on a five-member board before such a momentous decision to privatize this industry, when one of the five board members asked for a national security briefing before that final decision was made that that board member would be denied getting such a national security briefing? Does that seem appropriate?

Mr. GENSLER. The role of Treasury was to review; and as I said, we were very much in touch with the national security part of the administration, the National Security Council, the NSC, the State Department, CIA, Department of Energy on these matters. The board deliberations as Congress had set up were separate from the deliberations. We were not—I was not party to that board meeting that you are referring to. And if board members requested that, it was certainly amongst the board members. This would be the first time I would be familiar with that.

Mr. STRICKLAND. I would hope you would feel disappointed to know that Mr. Rainer was using a conversation that he had had with you as a way of denying such a briefing.

One further question, if I could, Mr. Chairman. Mr. Gensler, I think you say in your testimony that privatization occurred as a result of the unanimous vote of the board, and I think it is important for us to understand that on that five-member board, three members voted to privatize, one member abstained, and one member voted no. This was a decision that was made in a conflictual atmosphere, and it was an important national security decision; and it seems to me that it was pushed forward, national security concerns were put by the wayside and even a Senator, even a Senator writing a letter raising national security concerns was, for all practical purposes, just ignored in order to get this privatization taken care of as quickly as possible.

Mr. GENSLER. If I could just respond to help out a bit. If I in any way left you with the wrong impression, I didn't mean to. The vote of the board in June 1998 on whether to move forward with the privatization through the initial public offering or the leverage buyout proposal was actually a unanimous vote. I think the vote that you are referring to was on the pricing, on the day of the pricing when the road show had been completed after about a month, at that point in time, which was the split vote.

Mr. STRICKLAND. Thank you.

Mr. WHITFIELD. Thank you. I have a couple of more questions, and then Mr. Stupak and Mr. Strickland if you have a couple more, and then we will dismiss this panel.

Mr. Moniz, October 27, 1999, Mike Telson, this is in document 17, has a memorandum to the Deputy Secretary. This is in conjunction with USEC's request for a $200 million appropriation from the government because of the money that they calculated they were losing by implementing the agreement with the Russians. In this document USEC calculates what it would cost them to enrich 5,500,000 SWU. And then the Department of Energy calculated what they thought it would cost them to enrich 5,500,000 SWU. According to this document, DOE's calculation was twice per SWU what the USEC calculation was. Is it true that you used that document as one of the factors in deciding not to pursue the $200 million appropriation?

Mr. MONIZ. There were several inputs in the discussion at that time period, including—this probably comes from the analysis that the Department had performed. The analysis that was done, and I must stress that was not a validated analysis. In fact they did not have access to all of the data from either the corporation or from the Department of Energy. This was a group that was familiar with the industry. We felt we could still learn something from that. They clearly came out with results that were quite different from some of the USEC analyses. I am not sure if those discrepancies have been fully resolved, but clearly one of them in the discussion involved power issues.

Mr. WHITFIELD. Would you agree that USEC is the beneficiary of very low kilowatt hour costs?

Mr. MONIZ. We have the government contract which gives them a significant amount of very low-cost power, although not all their power is low cost and that becomes the issue at the margin. If it then goes to much higher cost power, the implications are very, very significant.

Mr. WHITFIELD. Implications are catastrophic, really.

Mr. MONIZ. One cent per kilowatt hour additional cost translates into $25 additional per SWU, so it has a significant impact.

Mr. WHITFIELD. Which can be disastrous.

Mr. MONIZ. Right. In the end, the Secretary had some exchanges by letter with Mr. Timbers. We performed analyses, had discussions with the corporation. In the end we clearly came to the conclusion that the HEU Agreement was an asset for USEC, and again all I can say is that their decision, presumably a business decision in my view, supports the idea that it is a net asset.

Mr. WHITFIELD. Mr. Gensler, if USEC tomorrow made the announcement that they intended to close the Paducah plant or the Portsmouth plant, what would Treasury do?

Mr. GENSLER. Well, I think under our arrangements, they need to come to us before they make such announcements. We have put them on notice of that, and I think they understand we have had dialog with their lawyers on that matter as well. So I think the time to talk with Treasury is before such announcement, and they have indicated they understand that full well.

Mr. WHITFIELD. At this point they have had no discussions with you about this.

Mr. GENSLER. That is right.

Mr. WHITFIELD. Mr. Stupak.

Mr. STUPAK. Thank you. Mr. Moniz, do you think the conversion industry in the United States should be eliminated?

Mr. MONIZ. No, I don't.

Mr. STUPAK. Then ConverDyn, should they just go out of business sooner rather than later then?

Mr. MONIZ. I have no basis to judge that. Certainly, I realize the conversion prices have fallen by more than a factor of two.

Mr. STUPAK. I want to discuss a little bit about that because the president of the Uranium Producers of America is going to testify later today that DOE's transfer of an equivalent of 11.6 million pounds of uranium through USEC with no restriction on when it could be sold, plus large amounts of uranium in USEC had accumulated by underfeeding, have destroyed the domestic uranium market as uranium is being sold at less than the cost of producing it. As you know, USEC has been actively selling its uranium inventory to generate short-term cash and earnings and the price has fallen. Do you agree with this analysis?

Mr. MONIZ. Certainly, that USEC has sold substantial amounts of uranium is a fact. As I said earlier, that has certainly been one of the factors in driving down the prices and causing the soft market.

Mr. STUPAK. Do you think Congress intended the domestic uranium industry should pay for the privatization of USEC?

Mr. MONIZ. Well, as stated earlier, first of all, the transfers of the Department's uranium to USEC upon privatization, first 56 percent flowed directly from EPAct. The remainder is authorized in the privatization act and counterbalancing that, the USEC Privatization Act was 31 million pounds of the total 73 million pounds of DOE uranium. Countervailing that, is that DOE has taken—in the context of the HEU Agreement 58 million pounds off the market.

Mr. STUPAK. But it hasn't lifted the price that much, though.

Mr. MONIZ. It certainly has not.

Mr. STUPAK. Apparently DOE and no one else knew that USEC had accumulated over 30 million pounds of uranium that it could sell without restrictions prior to privatization and that those sales would be pressed to markets. So why did DOE transfer uranium without restrictions on the sale?

Mr. MONIZ. Roughly half of the uranium transferred had restrictions or its entry into market.

Mr. STUPAK. How about the other 30 million? No one knew about it?

Mr. MONIZ. I don't know that in detail. I could get back to you for the record.

[The following was received for the record:]

From 1993 through 1998, the Department of Energy transferred about 172 million pounds of uranium in the form of natural uranium hexaflouride to USEC in order to meet requirements under the Energy Policy Act of 1992 (EPACT) and the USEC Privatization Act. Of the total 172 million pounds transferred, approximately 99 million pounds was customer-owned uranium. The remaining amount, of approximately 73 million pounds represents the Department's transfers of its uranium to USEC.

Forty-two million pounds or about 57 percent of the total DOE transfers of 73 million pounds was restricted by law or agreement in terms of the manner in which it can be introduced into the uranium market. While the 31 million pound difference was not market-restricted, the majority of it—about 22 million pounds—represented the Department's working inventory for non-government operations and became USEC Inc's initial working inventory. The transfer of the working inventory—a requirement under the EPACT—occurred in 1993 and was the subject of a 1994 review by the General Accounting Office that concluded that the initial transfers had been completed consistent with the requirements of the EPACT. Another 0.9 million pounds of DOE's working inventory was transferred in 1995. The remaining 7 million pounds in uranium inventory transfers were accomplished over the next several years to satisfy other requirements of the EPACT. A table showing the transfers of uranium inventories follows:

Document	Date	MTU	Quantity of Uranium (Millions of lbs. of U_3O_8, equivalent)
EPACT TRANSFERS.			
Determination Order (interim)	7/1/93		
—customer owned uranium		37,982	98.75
—government owned working inventory		8,800	22.88
Subtotal, uranium initially transferred		46,782	121.63
Memorandum of Agreement (MOA)	12/15/94		
—HEU (USEC receives blended down LEU)		2,400	6.24
Determination Order (final)	11/21/95		
—adjustment for actuals in government owned working inventory		340	.88
Amendment to MOA FY98-1	5/15/98		
—Natural and low enriched uranium		[1]4,253	[1]11.06
Amendment to MOA FY98-2	5/15/98		
—correction in amount of HEU expected to be recovered by USEC		208	.54
Total, uranium transferred to meet EPAct		53,983	140.35
USEC PRIVATIZATION ACT TRANSFERS.			
Memorandum of Agreement	4/21/98		
—50 Metric Tons of HEU (To be delivered 1999-2004)		[2]5,000	[2]12.97
—7,000 Metric Tons of Natural		[2]7,000	[2]18.20
Total, uranium transferred to meet USEC Priv. Act		12,000	31.17
Total, uranium transferred to USEC		**65,983**	**171.52**
Less: customer owned uranium (transferred 7/l/93)		-37,982	-98.75
Net, uranium transfers from DOE to USEC		**28,001**	**72.77**

[1] The MOA restricts the introduction of the uranium into the market to not less than 4 years and no more than 35 percent in any one year. A Secretarial Determination of No Material Adverse Impact covering this transfer was signed by Secretary Peña on May 15, 1998.

[2] The USEC Privatization Act and the MOA restricted the introduction of the uranium into the market such that no more than 10 percent of the uranium could enter the market each year after 1997 or 4,000,000 pounds, whichever is less. The Act exempts this material from the Secretarial Determination requirement.

Mr. STUPAK. That is the problem. No one knew about it before; and it sounds like you know the answer, but you are not telling us.

Mr. MONIZ. No. I will tell you anything I know. I am afraid I don't know specifically about this 30 million pounds. Again, over half of the uranium transferred had very clear restrictions on sale into the U.S. market. The other issue, of course, is that within the restriction on their uranium sales, one certainly anticipates they would also make business decisions in terms of the overall market. And also I should add some of those sales have come from overseas.

Mr. STUPAK. But they need cash so they are selling at less than market value and really hurting the domestic industry because they got it basically for free?

Mr. MONIZ. I would say that in the privatization, there was a rather complex set of assets and responsibilities transferred. Part of it was inventories. Part of it was the power contracts. There were also responsibilities in terms of the restrictions on employment, the restrictions on the operation of the plant.

Mr. STUPAK. They basically got the uranium for free.

Mr. MONIZ. It was a transfer of assets and responsibilities that was judged in the private sector.

Mr. STUPAK. Was there monetary paid to the U.S. Treasury for that uranium end responsibility?

Mr. MONIZ. It was one of the assets in the privatization, and Treasury received $1.9 billion total when this private sector judged the set of assets and responsibilities.

Mr. STUPAK. They dump it when they want, drive down the private industry and the private market, and that is what we are experiencing now; and that is what the next testimony will be.

Mr. MONIZ. Some unrestricted and some restricted uranium.

Mr. STUPAK. Thank you, Mr. Chairman.

Mr. WHITFIELD. Mr. Strickland.

Mr. STRICKLAND. Thank you. Mr. Gensler, just one more question. Is USEC legally obligated to inform you that a significant event has occurred; and if USEC chooses to close a plant without informing you, is there any legal reason why they should be required to inform you? Is there anything in the Treasury agreement that legally binds USEC to inform Treasury that a significant event has occurred?

Mr. GENSLER. Let me say again I am sorry because that was our counsel. We think that it is most definitely implied in our contract. We so informed them in our dialogs with them counsel to counsel. They have understood that and as I said earlier haven't come to us at this point in time, but there has been no debate when we have talked to them about that.

Mr. STRICKLAND. I guess my response would be this is an important transaction, and I would hope that there would have been some with all due respect to your legal counsel someone associated with Treasury that would know how to write a binding legal contract which would have made such an obligation very clear.

Dr. Moniz, one of my favorite people as a matter of fact.

Mr. MONIZ. Thank you.

Mr. STRICKLAND. This is my question. Under Public Law 104-134, the USEC Privatization Act section 3108, which deals with the effect of the transfer of contracts, isn't it true that the Government remains obligated to the parties—and by parties I mean customers or consumers with whom USEC contracts—even if USEC breaches

these contracts so that in effect the Government is the guarantor who is on the hook for any of USEC's actions?

Mr. MONIZ. As you know, I am not a lawyer; and I would like to clarify this to make sure it is correct. I believe this is correct that we have a liability there.

Mr. STRICKLAND. So these provisions basically relieve USEC of any——

Mr. MONIZ. If I may add. Yes, sir, unless the contracts are changed.

Mr. STRICKLAND. So these provisions relieve USEC of any ultimate accountability to those with whom they contract?

Mr. MONIZ. Well, presumably to run a viable business at least, they would want to be honoring their contracts.

Mr. STRICKLAND. Well, other scenarios where they may for some reason choose not to continue to operate a viable business.

Mr. MONIZ. It is not for me to speculate on that at the moment. Again, I would just repeat that from our perspective, I think there are three critical public equities for us to pay attention to and quite frankly be concerned about: the operation issue, the security of supply issue, and the commitments to the communities and workforce in Paducah and Portsmouth.

Mr. STRICKLAND. The reason I raise the question with you, because we say privatization was something that was widely supported and a good thing, but at the end of the day it is Uncle Sam, it is the taxpayer that ultimately is still accountable for any decision that USEC makes; and that is one of the reasons I continually find myself asking why privatization.

Mr. Paperiello, when you make your analysis, will the Russian material be counted as supply in determining a reliable supply of enrichment during your review of these matters?

Mr. PAPERIELLO. I don't know. I mean, I am sure people on my staff do. I just don't know.

Mr. STRICKLAND. It seems to me that if the requirement is to have a reliable domestic supply that we ought not to be able to count as a part of that supply material coming in from a foreign source subject to changes within the Russian Government or any number of other circumstances. Will you investigate that question and provide us with an answer?

Mr. PAPERIELLO. Yes, sir.

[The following was received for the record:]

In NRC's financial review, we are looking at business plans, contracts, and other related documents in order to conclude whether USEC will have the ability to continue operating and thus provide a "reliable and economical source of domestic enrichment services." With respect to contractual commitments, uranium downblended by Russia from the HEU Agreement once it has entered the U.S. market will be considered as a non-domestic source for filling USEC contractual commitments. The financial effects on USEC of the requirement for it to be the Executive Agent for the Russian HEU Agreement will be reflected in USEC's financial projections and will be a part of our review.

Mr. WHITFIELD. Mr. Strickland, one more question. I would like to remind Mr. Paperiello, emphasize that we very much would like to have an answer to that question.

Mr. PAPERIELLO. Yes, sir.

Mr. STRICKLAND. One final question quickly. If after you do your analysis, which I am sure will not be made available public, but

you will submit this analysis to the commission, if your findings are such that you are unable to tell the commission that USEC in your judgment as a result of your analysis is unable to continue to be a reliable supplier of domestic product, what are the choices that face the commission under the law?

Mr. PAPERIELLO. I think our major option is to inform the administration and the Congress. If you think of our authority, I can revoke or suspend the certificate. That would mean the plant couldn't operate. So, therefore, you wouldn't have a domestic supply. As a regulatory safety agency, we are sort of in a—this is an unusual situation for us to be in.

Mr. STRICKLAND. That is why I think it is important for this committee and for this Congress to understand that if you reach such a determination and you cannot legally license or certify these plants for continued operation, the only reasonable thing to happen in my judgment is for this government to once more assume ownership and control of this industry because we cannot allow these plants simply to continue to cease functioning. And I just point that out because I think that could be a very real possibility and that as a government, as I said earlier, we cannot allow this industry to fail; but we can allow this corporation to fail.

Thank you, Mr. Chairman. I turn back my time.

Mr. WHITFIELD. I want to thank this panel for your statements and answering our questions. We may have some additional questions that we will get to you and would hope that you would respond to those in writing. This panel is dismissed. Thank you very much.

I will now call the third panel: Mr. James Graham, president of ConverDyn; Dr. Shelby Brewer, president of S. Brewer Enterprises; Mr. Richard Miller, policy analyst for PACE International; Mr. Mark Stout, vice president, Uranium Producers of America; and Dr. Joseph Stiglitz with the World Bank.

The Chair would advise each of you that under the rules of the House and rules of the committee, you are entitled to be advised by counsel. Do any of you desire to be advised by counsel during your testimony here today? The anticipated response is no. In that case, if you would please rise and raise your right hand, I will swear you in.

[Witnesses sworn.]

Thank you all very much for being with us this afternoon. We genuinely appreciate your coming to testify. All of you are well versed on this issue, and we look forward to your testimony. Mr. Graham, if you would like to start.

TESTIMONY OF JAMES J. GRAHAM, PRESIDENT, CONVERDYN; MARK STOUT, VICE PRESIDENT, LAND AND MARKETING, URANIUM PRODUCERS OF AMERICA; SHELBY T. BREWER, S. BREWER ENTERPRISES, INC.; JOSEPH E. STIGLITZ, WORLD BANK; AND RICHARD D. MILLER, POLICY ANALYST, PACE INTERNATIONAL

Mr. GRAHAM. Mr. Chairman and members of the subcommittee, my name is Jim Graham; and I am the president and CEO of ConverDyn, and I would like to thank you for the opportunity to participate on behalf of the U.S. domestic conversion industry. For

the sake of brevity, I have submitted my written testimony and will speak along some key issues and points for our business and really would state that the situation of the conversion industry today is one of desperation. This should be a time of optimism because in 1999 the U.S. industry elevated their record output of electricity from the nuclear industry to over 23 percent. But instead we may be witnessing a demise of the conversion industry and of the nuclear fuel cycle here in the United States.

ConverDyn is the sole provider of conversion services in the United States. Conversion is just a chemical process of converting U308, an oxide and UF6, a gas. It is a small component, less than 4 percent of the nuclear fuel cycle cost; but it is a critical component in the fuel cycle. Our facility in Metropolis, Illinois, is the only facility as I mentioned and represents 60 percent of the conversion capacity in North America. We are one of five in the world. The future of the facility and the 350 remaining workers and more importantly a secure domestic supply of nuclear fuel for the U.S. industry today is in doubt. Primarily two actions by the U.S. Government has placed our industry in peril: first, the HEU Agreement between the governments of the United States and Russia and, second, the privatization of the U.S. Enrichment Corporation.

The HEU Agreement was fully supported by ConverDyn and its parent companies, and we continue to support that agreement today. The second, privatization of U.S. Enrichment Corporation, occurred almost simultaneously with the HEU Agreement. The key point here, had, one, the HEU Agreement been signed and supported by all, the industry today would be okay in our opinion. But simultaneously these two events and aggressive action of marketing the material transferred to U.S. Enrichment Corporation has basically put our industry at peril. An example is the HEU Agreement. Over the next 15 years, the annual amount of conversion services delivered into the United States is almost the same output from our conversion facility in Metropolis, Illinois.

Unfortunately, the commercial fuel created by the HEU Agreement is sold primarily into the United States market. It has not in Europe. Ias not in Asia. It is all in the United States. For 50 years the U.S. Government has been a good participant in the U.S. nuclear industry but never as a competitor. With the privatization of the U.S. Enrichment Corporation, a competitor to both the conversion industry and the uranium industry was created overnight. This company at privatization had an inventory in excess of 28,000 metric tons of conversion services. This is the equivalent of almost 3½ years of output from our facility. Their cost basis of this material was basically zero. There is no cost basis.

I have an interesting chart that I would like to show to illustrate the points of our industry, if I may. This first chart shows the decline in price for the conversion services over the last 3 years. You can see the decline in the last 2 years were very dramatic; and you can see the events, privatization of the U.S. Enrichment Corporation and the HEU Agreement, both impacted.

The next chart shows the annual sales, forward sales for ConverDyn; and you can see that two occurrences, primarily the U.S. Enrichment Corporation, you can see the decline in our forward sales as an industry in the United States. The next chart

shows the same period of time that the sales from the U.S. Enrichment Corporation of their uranium and conversion into the marketplace. This information is obtained from their own annual reports, 10-Ks, 10-Qs, and public information. It is this decline in our own business sector and a growth of the new competitor that is basically putting our industry in peril.

The continued loss of ConverDyn of sales from this aggressive government-created competitor may make it uneconomical for us to continue. We estimate at the current rate of sales by the U.S. Enrichment Corporation that their inventory may be exhausted in 3 to 4 years. The problem is ConverDyn and our facility in Metropolis, Illinois, may not survive that long. We are in this business to make money and to survive. In the future if we are gone, the need will be there for conversion but the Metropolis plant may not be. So, Mr. Chairman, the combination of these two sources of conversion services, the Russian HEU and the transfers of material from DOE, is a burden that the sole U.S. domestic supply of conversion services cannot bear. Without relief, the demise of our industry is very likely. Thank you.

[The prepared statement of James J. Graham follows:]

PREPARED STATEMENT OF JAMES J. GRAHAM, PRESIDENT AND CEO OF CONVERDYN ON BEHALF OF THE DOMESTIC URANIUM CONVERSION INDUSTRY

Mr. Chairman, and Members of the Subcommittee, my name is Jim Graham and I am the President and CEO of ConverDyn. I would like to thank you for the opportunity to speak before you today on behalf of the U.S. domestic uranium conversion industry. The situation for the uranium conversion industry is one of desperation. In 1999, nuclear power generated a record twenty three percent of the electricity output for the United States. This should be a cause for optimism, but instead we may be witnessing the end of the domestic nuclear fuel cycle industry.

ConverDyn is the sole manufacturer in the U.S. uranium conversion industry. Conversion is the chemical process by which the form of uranium is changed from U308 to UF6 and is a small (representing less than 4% of the fuel cycle cost) but critical chemical step in the production of nuclear fuel for electric power production. Our facility in Metropolis, Illinois is the only such production facility in the U.S. and represents approximately 60% of the conversion capability that exists in North America. The future of this facility, its 350 remaining workers, and more importantly a secure domestic supply of nuclear fuel for the U.S. industry are in doubt.

Unfortunately, there have been two actions by the U.S. government, which have placed the future of this facility in peril. The first was the agreement between U.S. and Russian governments (the HEU Agreement) to turn former Soviet nuclear weapons into fuel for commercial reactors. ConverDyn and its affiliated parent companies supported and continue to support this effort. The second was the privatization of the United States Enrichment Corporation. These occurred almost simultaneously in the U.S. and placed undue burden on the domestic industry. One of these events could have been dealt with in the normal commercial environment, but both events together have forced the domestic uranium conversion industry out of balance and at great risk of being eliminated.

The HEU agreement will turn former Soviet nuclear weapons material into commercial nuclear fuel for the next 15 years. This creates an annual quantity of nuclear fuel in the U.S. nearly equal to the yearly output of the Metropolis facility.

U.S. & Russia HEU Agreement

Delivery Schedule vs ConverDyn Production

(MTU @ UF_6)

Year	gLRussian	ConverDyn
1996	3,636 Actual	11,600
1997	5,454 Actual	11,500
1998	7,300 Actual	11,600
1999	4,545 Actual	9,300

U.S. & Russia HEU Agreement—Continued

Delivery Schedule vs ConverDyn Production

(MTU @ UF_6)

Year	gLRussian	ConverDyn
2000	9,100 Projected	9,300
2001	9,100 Projected	9,300
2002	9,100 Projected	9,300
2003	9,100 Projected	9,300

The reduction of nuclear weapons is a cause that should be supported economically by the entire country. Unfortunately, the commercial nuclear fuel created by the HEU program is sold into the U.S. market to the detriment of the established commercial processing facilities, such as the Metropolis facility.

However, the HEU agreement by itself would not have significantly impacted the domestic industry. It was the subsequent privatization of the United States Enrichment Corporation (USEC) that has placed the domestic uranium conversion industry at risk.

For more than fifty years, the U.S. government has been a participant in the U.S. nuclear industry, but never as a competitor. Almost overnight, the U.S. government created a new competitor in the U.S. for uranium and conversion companies as a result of this action. Specifically, the privatization of USEC created a private company whose primary liquid asset is the 28,000 plus metric tons equivalent of UF6 transferred at privatization by DOE. This is the product of ConverDyn and as such, does not require conversion. USEC was privatized with enough former U.S. government inventory to replace almost three years of production from the Metropolis facility.

USEC Inventory At Privatization

(MTU @ UF_6)

Year	USEC	ConverDyn
1998	28,000+	11,500
1999	?	9,300
2000	?	9,300
2001	?	9,300

Public documents from USEC indicate that this former U.S. government inventory is being sold aggressively to the commercial nuclear industry as direct competition to the Metropolis facility contrary to what the government intended in the Privatization Act of 1996. (Attachment 1).

The USEC UF6 inventory has no cash cost and since privatization, USEC has been aggressively selling their inventory and obtaining a significant portion of conversion market share and revenue from the industry. Continued loss of sales by ConverDyn to this aggressive government created competitor may make it uneconomical to continue to maintain the Metropolis facility. We estimate that at the current rate of sale, this inventory will be exhausted in approximately 3 to 4 years. At that time conversion services from a facility like Metropolis will again be needed by the U.S. nuclear industry. However, unless some action is taken in the interim, the ConverDyn facility is likely to be shut down. Attachment 2 of this statement describes proposed remedies.

Mr. Chairman, the combination of these two sources of conversion services—Russian HEU imports and USEC transfers from DOE—is a burden that the sole U.S. domestic provider of primary uranium conversion services cannot bear. Without relief, the demise of the only domestic conversion provider, ConverDyn, is likely!

BACKGROUND

What is uranium conversion and what is its role in nuclear power?

Uranium conversion is a process of chemical transformation by which natural uranium concentrates in the form of U3O8 are converted to natural uranium hexafluoride (UF6). Uranium conversion is one of the four major steps in the production of nuclear fuel. These steps are components of the nuclear fuel cycle illustrated herewith.

1. Uranium Production—Uranium is a naturally occurring element in the earth's crust. When sufficiently concentrated by natural physical and chemical forces, it may be economic to mine the ore by open-pit, underground methods. Uranium is typically recovered from the ores by alkaline or acid leaching. Uranium is also produced by in-situ leaching and as a by-product of phosphate fertilizer, gold, and copper. The final product of uranium mining and processing is usually a mixture of uranium oxides referred to as either natural uranium concentrates, U3O8, or "yellowcake." Natural uranium concentrates contain 0.711 percent 235U, the active isotope in the nuclear process. The remaining 99.3 percent is the inactive isotope 238U.

2. Uranium Conversion—Natural uranium concentrates in the form of U_3O_8 are converted to natural uranium hexafluoride (UF_6) in order to provide an appropriate feed material for the next step in the nuclear fuel cycle: enrichment. The conversion process includes feed preparation, reduction with hydrogen to UO_2, hydrofluorination to UF_4, fluorination to UF_6, which is a gas at moderate temperatures and purification. Uranium in this form retains the natural isotopic concentration of ^{235}U of 0.711 percent.

3. Uranium Enrichment—Enrichment is a process of concentrating the ^{235}U isotope to higher levels of 3 to 5 percent in order to increase the efficiency of the fuel for nuclear reactors. Concentration of the ^{235}U isotope occurs by molecular weight in the gaseous diffusion process used in the U.S. and Europe, as well as in the centrifuge process used in Russia and Europe.

4. Fuel Fabrication—Enriched uranium hexafluoride is converted by fabricating companies to UO_2, pelletized, and inserted into zirconium alloy tubes which are then combined into bundles of nuclear fuel.

Each of these steps must be completed in order to produce a final product. Each step in the production process has a different character, different participants, different regional distribution, and a different value. These characteristics are referred to as the "Industry Value Chain." It is notable that most of the world's nuclear fuel cycle participants are foreign-owned, yet the U.S. is the world's largest user of nuclear fuel with over one hundred operating nuclear units.

Impact of HEU Agreement and USEC Privatization.

The sole manufacturer in the U.S. domestic uranium conversion industry is ConverDyn. Today, ConverDyn is being threatened by two recent actions by the U.S. Government:

1) The U.S.—Russian agreement on the conversion of highly-enriched uranium (HEU) in Russian nuclear weapons to nuclear fuel; and
2) The Privatization of the United States Enrichment Corporation.

Impact of Russian HEU Agreement—Nuclear warheads contains the same three components as nuclear fuel: 1) natural uranium concentrates, 2) conversion services, and 3) enrichment services. When the U.S. government devised a plan in 1995 to subsidize the dismantlement of Soviet nuclear weapons, the enrichment services component of those weapons received the bulk of the attention since it accounts for the bulk of the value.. Unfortunately, this plan failed to fully address the disposition of either the natural uranium concentrates component or the conversion components. As a government corporation, USEC was appointed as Executive Agent for the implementation of this plan. Ultimately, in 1999, an agreement for disposition of uranium concentrates was reached between three western, but non-U.S., companies and the Russian government. This agreement provides a defined structure for the disposition of uranium, but, again, no format for the disposition of conversion addressed. As a result, conversion is available from a variety of uncontrolled sources, which disrupt the stability of the industry.

The quantity of natural uranium concentrates and conversion services contained in dismantled Russian nuclear warheads amounts to approximately 9.1 million kgU as UF6 per year. Not all of this material can be sold in the U.S. each year due to the existing quota provision, but it is imported physically and is seen by nuclear utilities as a vast resource which will provide an abundant supply of uranium, conversion and enrichment far into the future. The U.S./Russian HEU agreement provides for the enrichment component to be used by USEC. The USEC Privatization Act specified that natural uranium concentrates could enter the country only in gradually increasing quantities. No limitations of any kind were applied to conversion services. ConverDyn attempted during the drafting of the Privatization Act to obtain the same quota provisions provided to the natural uranium component but was advised by the government that we were considered a monopoly. ConverDyn protested unsuccessfully that the U.S. market was truly international and that all primary conversion providers have access to the available U.S. market.

Impact of the USEC Privatization—When USEC was privatized, it received a substantial endowment of both uranium concentrates and conversion services contained in excess of 28,000 metric tons of uranium hexafluoride. This endowment was designed to provide USEC with a working inventory, to fund certain clean-up operations and to provide sufficient assets to ensure that the privatization process would be well received by investors. Both in terms of the privatization process and certain of the transfers of material to USEC, some strings were attached to prevent dumping of USEC products. These strings included limitations on the annual sales of the natural uranium concentrates transferred to USEC. No restrictions, however, were placed on sales of the conversion services contained in those transfers.

In its S-1 registration statement of June 29, 1998, USEC published its plans to sell most of its inventory between 2000 and 2005. USEC's CEO Mr. William Timbers later stated that these sales would amount to less than 10 percent of the world requirements. USEC's major sales arena, however, is the U.S. and 10 percent of world requirements equates to approximately 40 percent of U.S. requirements. Even worse, a large portion of U.S. requirements for that period have already been filled. Hence, there is little or no room for additional sales by others, especially a newly created competitor with significant cash needs. Since most of these sales are to be in the form of UF6, the U.S. conversion industry is suffering a crippling blow.

USEC does not seem to understand the impact of sales of this magnitude on the nuclear fuel components industries. In a July 27, 1998 letter to the State department, Mr. Timbers stated: "USEC will dispose of natural uranium in a gradual and flexible manner so that the company, as well as all participants in the global uranium marketplace, can benefit from the maintenance of a healthy uranium market." A few months later, Mr. Timbers further stated: "We will dispose of our uranium inventory in a gradual market-sensitive manner." Reality has proven this not to be the case.

Prices Have Fallen—Conversion prices in the spot market fell from $6.00 per kgU as UF_6 in 1997 to $2.45 in early 2000. Primary supply has remained unchanged during this period while at the same time consumption has increased slightly, but secondary supply from U.S. Government inventories transferred to USEC pursuant to the privatization process and from converted Russian nuclear weapons has entered the market in massive quantities. Historically, the uranium conversion business as been supported by long term contracts. The volume of activity in the spot market remained less than ten percent until the early-nineties when secondary supplies started to impact the market increasingly. Additionally, long-term prices were historically higher than spot prices and did not follow the spot market activity until the last several years. The market dynamics created by an aggressive government-created competitor in the market place has forced the long-term market value down and forced the long-term prices to nearly track the spot market.

Sales Have Dropped—The primary conversion sales volume has been cut to less than half of the 1997 level. Aggressive sales at below market prices by USEC has reduced the amount of material sold through the competitive bidding process as utilities obtain more and more material in "Off-market" transactions at discount prices.

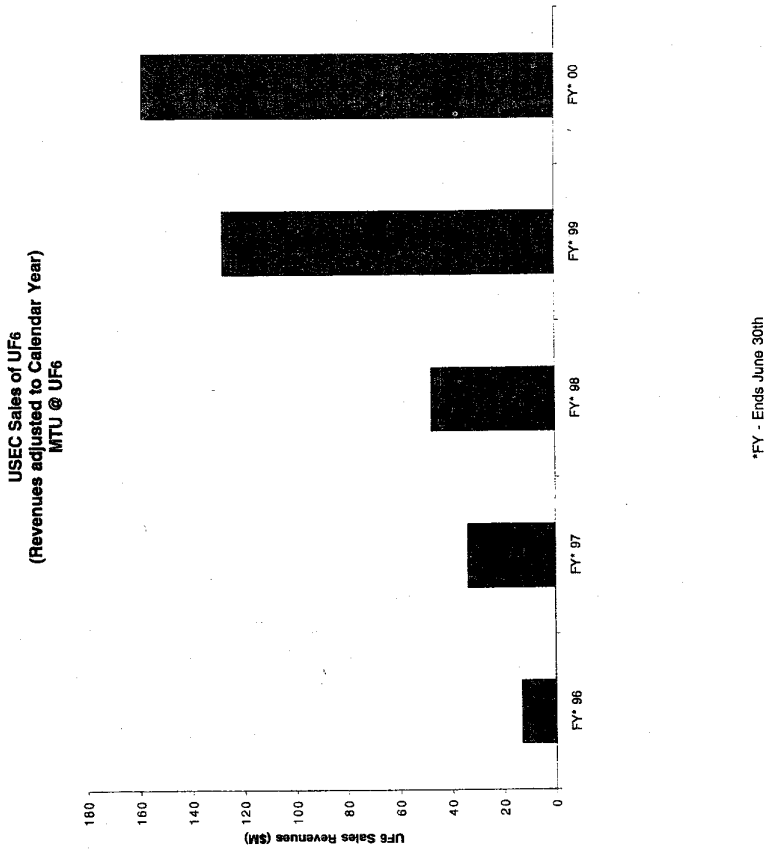
Revenues Have Collapsed—As a consequence of reduced prices in combination with reduced volume; revenue expectations for the domestic uranium conversion company have been cut by a factor of four.

Unfair Competition—HEU and USEC inventories of conversion services have no current cost basis. Uranium conversion services contained in the converted Russian HEU were produced by the Soviet Union in the distant past for military purposes. Conversion services currently being marketed by USEC were produced by the U.S. government over the past half-century as strategic and working inventories. Primary converters such as ConverDyn, which have current costs for labor, chemicals and electricity, cannot compete with this supply. These old inventories are valued at market price and there is no loss to be incurred or reported no matter how low the price goes. At present market consumption rates, the USEC UF6 inventories will significantly impact the market for another three to four years.

Importantly, the USEC Privatization Act itself makes it clear that the impact on the domestic uranium conversion industry shall be monitored and that action is to be taken **"to prevent or mitigate any material adverse impact on such industries."**

To date, it is clear that if any such monitoring has been done, it has missed the indisputable and devastating impact that the privatization has had on the conversion industry. In fact, prior to and since privatization, the conversion industry has not even been consulted. Further, and almost needless to say, no action has been taken to mitigate the impact on our industry.

ATTACHMENT 1



ATTACHMENT 2

POTENTIAL U.S. GOVERNMENT ACTIONS TO SAVE THE DOMESTIC NUCLEAR FUEL CYCLE

Proposed Remedies—Mitigation of the impact of USEC and/or the HEU UF6 sales may be easily accomplished by a combination of the following:

1. Amend the Privatization Act to eliminate unfair competition from conversion services contained in converted Russian HEU. Such competition may be mitigated by including conversion services in the already established quota for the contained uranium. Such a quota would not impact the implementation of the HEU deal; rather it would ensure that resultant materials did not severely impact the U.S. market.
2. DOE could purchase the remaining uncommitted portion of the USEC UF6 inventory for a negotiated market value. This would provide DOE with an asset that could be sold later at a greater value and at such time as a Secretarial determination could show that release of incremental portions would not have a major impact on the marketplace.
3. Alternatively, DOE could borrow the uncommitted portion of the USEC UF6 inventory at a negotiated interest rate and return to USEC for sale (not delivery) at such time as a Secretarial determination could show that release of incremental portions would not have a major impact on the marketplace. Such a plan preserves the inventory as an asset for USEC, yet provides a means for it to earn current revenue. Certainly, just withholding the material from the market will increase the asset value and provide for even greater interest payments.
4. DOE could purchase an amount of conversion services for a four-year period of time at a negotiated price to assure the viability of the sole domestic uranium conversion facility. DOE would be able to sell the conversion at such time as a Secretarial determination could show that release of incremental portions would not have a major impact on the marketplace.

ATTACHMENT 3

CONVERDYN: HISTORY AND FACILITIES

In November 1992 affiliates of Honeywell and General Atomics formed ConverDyn, a 50-50 partnership to more effectively market the uranium conversion services provided by Honeywell's Metropolis, Illinois plant. This facility has operated since the late 1950's. Both Honeywell and General Atomics are U.S. companies that have been in existence for more than 50 years. Honeywell is a publicly held corporation listed on the New York stock exchange while General Atomics is a privately held company.

ConverDyn's major activity is the supply of UF_6 conversion services to its nuclear power utility customers worldwide. The major activity at the Metropolis facility is the production of UF_6 and related services.

Production Capacity—Annual production capacity is 12,700 mtU as UF_6.

History of Production—Metropolis production has increased steadily over the years commensurate with our customers' demands. Production was curtailed to 8.2 million kgU as UF_6 in 1999 from 12.7 million kgU due to deteriorating market conditions.

Property and Personnel—The Metropolis Works is located on 1,000 acres of property with the actual operation occupying 50 acres with the balance in farms and woodlands. Approximately 350 people are employed at the plant; total annual payroll exceeds $16 million. The Company place strong emphasis on excellence in performance especially in the areas of safety, environmental and regulatory matters. Metropolis Works sets the standard for safety and environmental/regulatory performance in its industry. Its personal injury record is consistently better than the chemical or nuclear industries as a whole, and it enjoys a good relationship with all regulatory agencies, including Environmental Protection Agency, Occupational Safety and Health Administration, and the Nuclear Regulatory Commission. The UF_6 operation is conducted under NRC License, SUB-526.

Product Quality and Performance—UF_6 production quality is 99.99% and has been consistently supplied to all Western enrichment facilities. The Metropolis facility was among the first plants to receive ISO-9000 certification at Honeywell. The UF_6 quality assurance program includes formal operating procedures and operator training, as well as preventive maintenance for process equipment and assurance programs for cylinders and laboratory equipment and instrumentation.

Mr. WHITFIELD. Mr. Graham, thank you.

Mr. Stout, if you would give your statement. We will try to keep these to about 5 minutes.

TESTIMONY OF MARK STOUT

Mr. STOUT. Mr. Chairman, members of the committee, my name is Mark Stout. I am vice president of marketing for Rio Algom Mining Corporation and president of the uranium Producers of America.

Mr. Chairman, Congress has repeatedly recognized the importance of maintaining a healthy domestic uranium industry. In the 1992 Energy Policy Act, Congress mandated that U.S. Government stockpiles must not be introduced into the commercial marketplace in a manner that would adversely impact the domestic uranium industry. That principle was reiterated again in 1996 in the USEC Privatization Act. Nevertheless, domestic production has declined by 50 percent, and the value of uranium assets worldwide have plummeted in the 2 years since USEC was privatized. The principal cause is the Department of Energy has failed to meet their congressional mandate to use U.S. Government stockpiles in a manner not detrimental to domestic uranium industry.

Two government initiatives which greatly influenced the precarious position we find ourselves in today: first, through the Russian HEU Agreement, our government has chosen to pay for its non-proliferation policies concerning former Soviet nuclear weaponry by requiring the commercial marketplace to absorb this material and bear the burden—most of the burden of the cost. Second, in an effort to maximize the value of the corporation—of the enrichment Corporation when it was privatized, huge government inventories were assigned to USEC before the corporation went public. The amount of U.S. Government uranium given to USEC is equivalent to about 25 times the amount of current domestic production.

Together these two initiatives have severely depressed the price of natural uranium. The depressed price threatens not only the viability of the domestic uranium industry, but ironically it also threatens the Russian HEU Agreement. It was clearly foreseen in 1995 by sponsors of the USEC privatization that a balance needed to be achieved in metering into the U.S. and western markets Russian HEU uranium and U.S. Government uranium transferred to USEC.

During 1995 representatives of the domestic uranium industry and USEC met congressional staff and DOE to work out a reasonable schedule for the sale of Russian HEU and USEC uranium. The results of these discussions were incorporated into the 1996 USEC Privatization Act. The privatization act limited to approximately 31 million pounds the amount of uranium to be transferred to USEC and restricted annual USEC uranium deliveries in the U.S. to no more than 10 percent of the amount transferred or 4 million pounds, whichever was less.

In April 1996, President Clinton signed the privatization act. Shortly thereafter, USEC began to market uranium far more aggressively and in much greater quantities than envisioned. The USEC S1 registration statement filed with the SEC over 2 years later revealed publicly for the first time that about two and a half times the amount of uranium inventory allowed in the privatiza-

tion act was to be transferred to USEC and that USEC's projected sales volume would far exceed the limitations set forth in the act.

After reviewing the surprised disclosures contained in the S1, Senator Domenici expressed concern over the impact of the additional transfers on both the uranium market and on the Russian HEU Agreement. He urged the National Security Council to review the impact of these transfers prior to the administration's decision to approve the sale of the enrichment corporation. Shortly thereafter, Senator Domenici explicitly requested the administration not to transfer the excessive uranium to USEC. Senator Domenici's recommendations were not taken. The results of the excessive government transfers have been production curtailments, mine closures, termination of development plans, departure of critical talent, layoffs, large asset write-downs and a total cessation of expiration by every uranium mining company in the U.S. and most overseas, for that matter.

When President Clinton signed the privatization act, the price of uranium was $16.15 per pound on the spot market. Since that time it has now dropped to about $9.10 a pound. Domestic production in 1996 totaled 6.3 million pounds. This year we will be lucky to make 3 million pounds. Perhaps even a better measure of what the USEC privatization has meant to our industry which is reflected in the CAMECO which is the largest publicly traded uranium company in the world stock price which has declined from $72.90 in April 1996 to 16.80 at last week's close of the foreign exchange, a loss of some 80 percent of its value. The domestic uranium industry cannot survive for much longer the uncontrolled dumping of transferred U.S. Government stockpiles by USEC.

Mr. Chairman, we urge this committee to look into why the quantities of uranium transferred from DOE to USEC increased so dramatically from the time the initial privatization plans were agreed to in 1995 and into the details of USEC's sales activities today, especially in light of a report issued earlier this week by the bank of New York that cites USEC-estimated uranium sales totaling over 67 million pounds through fiscal year 2006, an amount which would seriously limit the ability of Russian HEU uranium and U.S. uranium to enter the market. We urge the committee to consider legislation, to reaffirm the intent of the privatization act with respect to USEC uranium transfers and sales and make it clear that USEC does not have legal immunity from taking actions contrary to the provisions of that act. Thank you.

[The prepared statement of Mark Stout follows:]

PREPARED STATEMENT OF MARK STOUT, PRESIDENT, URANIUM PRODUCERS OF AMERICA

Mr. Chairman and distinguished members of the Committee, my name is Mark Stout. I am Vice President, Land and Marketing, for Rio Algom Mining Corporation, and I currently serve as President of the Uranium Producers of America (UPA), a trade association of domestic uranium mining and milling companies. I am testifying today on behalf of the UPA.

Mr. Chairman, the domestic uranium producing industry has a remarkable and unique relationship with the United States Congress dating back to the enactment of the Atomic Energy Act in 1954. The uranium industry was created by the Federal Government to serve national security needs in the early years of the Cold War. Private industry responded admirably to the government's urgent need for uranium. After satisfying the national security need to fuel the nation's nuclear defense, the domestic industry became a reliable source for the country's nuclear power industry.

The domestic industry has established and maintains today valuable strategic resources. These resources include skilled operators, coveted technology and competitive uranium operations and reserves.

Congress has repeatedly recognized the importance of maintaining a healthy domestic uranium industry. When Congress addressed energy policy in the 1992 Energy Policy Act, it mandated government stockpiled uranium must not be introduced to the commercial marketplace in a manner that would adversely impact the domestic mining industry. That principal was reiterated again in 1996 in the United States Enrichment Corporation Privatization Act.[1]

Mr. Chairman, despite repeated efforts by Congress, the domestic uranium industry is rapidly becoming an endangered species. The Department of Energy has continuously failed to meet its charge to use U. S. government uranium stockpiles in a manner not to adversely impact the domestic uranium industry. As this committee considers the impact of recent U.S. government owned uranium transfers to USEC, we ask that a way be found to enforce and monitor existing uranium policy. Despite DOE's contention that its actions would have no adverse impact, the facts show the contrary. The U.S. is rapidly becoming totally dependent on U.S. and Russian government stockpiles and production from foreign producers. In our view, this is shortsighted energy policy and dangerous economic policy. This is true for any valuable natural resource commodity, especially one that fuels almost one-fourth of our nation's electrical generation.[2]

Two government initiatives have greatly influenced the precarious position in which the domestic producers find themselves today. First, our government has attempted to conduct its non-proliferation policies concerning former Soviet nuclear weaponry by requiring the commercial marketplace to absorb this material and bear the lion's share of the cost of its implementation. Second, in an effort to maximize the value of the Enrichment Corporation's privatization, large government inventories were transferred to USEC before the Corporation went public.

Together, these two initiatives have severely depressed the price of natural uranium. The depressed price threatens not only the viability of the domestic uranium industry, but ironically it also has negative implications on the U.S./Russian HEU Agreement, which is an important part of our national nuclear non-proliferation program.

More specifically, the transfer of DOE inventories to the United States Enrichment Corporation (USEC) has created devastating material adverse impacts on domestic uranium production due to the ensuing aggressive selling of these transferred inventories by USEC. According to the government's Energy Information Administration in 1998, USEC's level of marketable inventory approached 60 million pounds U_3O_8 equivalent. EIA stated this was enough to supply six-eight million pounds per year to the market roughly over the next decade. As shown by the chart attached as Exhibit 2, utility uncommitted demand cannot absorb these supplies, especially when Russian HEU uranium and conventional producers are interjected into the mix.[3]

Despite U.S. mining technology that allows domestic producers to compete in productivity with foreign producers, USEC sales have pushed the price of uranium below any valid cost of production.[4] USEC uranium sales combined with sales resulting from the implementation of other U.S. government initiatives have in effect "taken" the good faith investments made by domestic uranium producers. The adverse impact on the price of uranium from these secondary sources has severely impacted the domestic producers. We believe that the substantial damage to the producing industry is in direct contravention of the congressional mandate concerning the disposition of government uranium stockpiles expressed both in the Energy Policy Act of 1992 and the USEC Privatization Act.

Today we are faced with an extremely unusual economic situation in uranium. World uranium production is only one-half the demand for nuclear power reactor fuel. In 1999, uranium production was approximately 80 million pounds U_3O_8 compared to demand of 160 million pounds. This magnitude of a supply/demand imbalance is unprecedented in industrial commodity markets. Generally, in energy or

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[1] See Exhibit 1 (showing EPACT and Priv. Act. impact provisions).

[2] The most notable energy trend in the U.S. today is the continued electrification of our economy. Approximately 23% of electricity produced in the U.S. comes from uranium-fueled nuclear power reactors. At present, the majority of the natural uranium to be processed and fabricated into fuel for these reactors is supplied from foreign sources. Title X, Subtitle B of the Energy Policy Act of 1992 recognized the national need to avoid dependence on imports in this critical energy sector.

[3] See Exhibit 2 (Estimated Uncovered Uranium Requirements, 2000-2018).

[4] With the advent of *in situ* leach technology, U.S. production centers' productivity has compared favorably with foreign producers as shown on Exhibit 3.

metals markets an imbalance of only 1 or 2 percent will bring on substantial swings in the commodity price, as we have witnessed most recently with crude oil. This huge supply/demand imbalance in uranium, which has developed over the past ten years, is primarily the result of massive sales of Russian and U.S. government-owned inventories. In the early 1990's several hundred million pounds of natural uranium stockpiled in the Soviet bloc countries were dumped in Western markets.[5] By 1995, a major portion of these inventories had been absorbed. However, as natural uranium imports from the former Soviet Union declined due to consumption and as a result of "Suspension Agreements" limiting their entry into the U.S., Russian HEU (highly enriched uranium from dismantled nuclear weapons) began to be imported. It appeared in 1995 that Western markets could accommodate the deliveries of uranium purchases specified by the U.S./Russian HEU Agreement. This schedule called for natural uranium deliveries from HEU to be about eight million pounds U_3O_8 in 1995 through 1999, increasing to about 24 million pounds U_3O_8 in the year 2000 and beyond. As the HEU agreements were being finalized,[6] progressing along a somewhat independent path were plans to privatize the U.S. Enrichment Corporation. It was clearly foreseen in 1995 by sponsors of USEC privatization that a balance needed to be achieved in metering into U.S. and Western markets HEU uranium and U.S. government uranium inventories to be transferred to USEC.

During 1995, representatives of the domestic uranium producers and USEC met congressional staff and DOE to work out a reasonable schedule for the sale of HEU uranium and USEC's sales of U.S. government inventories. The results of these discussions were incorporated into the 1996 Privatization Act.[7] The Privatization Act that resulted from these negotiations limited to approximately 30 million pounds U_3O_8 the amount of uranium to be transferred from DOE to USEC and limited annual uranium sales by USEC to no more than four million pounds per year. The Privatization Act also specified the rate at which HEU uranium feed could be sold in the U.S. This schedule allowed two million pounds U_3O_8 of HEU uranium to be sold in 1998, increasing by one or two million pounds each year to a level of 20 million pounds per year in 2009 and beyond. The purpose of this section of the Privatization Act was to prevent the suppression of the price of uranium. This would benefit uranium producers and enhance the value of government stockpiles. It also served to promote long-term competitiveness.[8]

U.S. uranium producers supported USEC's privatization and believed that the limited transfers and schedules for uranium sales set forth in the Privatization Act provided a reasonable transition period during which the uranium production indus-

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[5] In the late 1980s, the Soviet Union began selling uranium in all forms into the Western World market at sales prices significantly below the production costs of all western producers. In response, in late 1991, a group of domestic uranium producers (the Ad Hoc Committee) joined by the Oil Chemical and Atomic Workers (OCAW) union filed an anti-dumping suit against the Soviet Union. About one month after the suit was filed, the Soviet Union dissolved and the case proceeded against the individual republics of Kazakhstan, Krygystan, Uzbekistan, Tajikistan, Ukraine, and Russia. The preliminary finding by the Department of Commerce ruled in favor of the Ad Hoc Committee and OCAW and determined that a dumping duty of 115.82% was appropriate. This extremely large dumping duty would have effectively precluded any imports of uranium from these republics. However, a provision of U.S. trade law allowed the U.S. government to settle these cases without domestic industry participation or agreement because these republics were considered non-market economy countries. Therefore, rather than letting the cases proceed to final dumping orders, in 1992 the U.S. Government entered into "Suspension Agreements" with Russia, Uzbekistan, and Kazakhstan. The "Suspension Agreements" set up CIS sales quotas legal in the U.S. as a function of market price, U.S. production, and other metering mechanisms. These republics were granted market quotas under the suspension agreements notwithstanding the prior determination that affirmed dumping. Since 1992, a total of almost 30 million lbs. U_3O_8 has been imported into the U.S. duty free from these countries.

[6] Once again, the Administration recognized the need to not adversely impact the domestic production industry in the U.S./Russian HEU Agreements. The Agreement provided that its implementation should be accomplished in a manner that minimizes impact upon the U.S. uranium industry. This position was ratified in a letter from the DOE Director of the Office of Nuclear Energy, Terry Lash, to Senator Craig Thomas in 1994. (See Exhibit 4.)

[7] See 42 U.S.C. 2297h-10

[8] "Privatization legislation should enhance the long-term competitiveness of the nuclear fuel markets. Long-term competitiveness means that the market includes multiple suppliers and avoids concentration of market power. * * * The [nuclear utility] industry believes that U.S. HEU transferred to USEC prior to privatization will provide some competitive advantage . . . The provisions which provide quantitative limits on the amount of material to be transferred and the rate at which the material can enter the market provides a useful framework for metering the introduction of the material to the market." Testimony of Joe Colvin, Executive Vice President, Nuclear Energy Institute, Before the Committee on Energy and Natural Resources, United States Senate, June 13, 1995 (USEC Privatization Hearing).

try and commercial markets could adjust to the implementation of the HEU Agreement and USEC privatization. Our support was misplaced.

In April 1996, President Clinton signed the Privatization Act. Shortly thereafter, USEC apparently began to market uranium far more aggressively and in much greater quantities than envisioned. The USEC S-1 registration statement filed with the SEC over two years later (shortly before privatization in the summer of 1998) revealed publicly for the first time that about two and one-half times the quantity of uranium inventory allowed in the Privatization Act was to be transferred to USEC and that USEC's projected sales volume would far exceed the limitations set forth in the Act.

THE USEC PRIVATIZATION ACT

In 1996, Congress passed the Privatization Act in order to authorize and facilitate the privatization of the enrichment program. Congress again recognized that USEC's ties with DOE posed a threat to private uranium producers and therefore built on the protections against the sale or transfers of U.S. government stockpiles mandated by the provisions of the Energy Policy Act.

Congress carefully included in the Privatization Act constraints on DOE's authority to transfer or sell uranium. Thus, § 2297h-10(a) of the Act first makes it clear that the "Secretary shall not . . . *transfer or sell* any uranium (including natural uranium concentrate, natural uranium hexaflouride, or enriched uranium in any form) to any person except as consistent with this section." DOE was authorized in the Act to transfer *without charge* up to 50 metric tons of HEU and 7,000 metric tons of natural uranium to USEC.[9] This transfer was the equivalent of approximately 30 million pounds of natural uranium. The legislative history indicates that this transfer was intended "as a means of enhancing the value of USEC in the marketplace and reducing DOE's costs of safeguarding surplus [highly enriched uranium].[10] In order to lessen the impact of USEC's sales of this transferred material, USEC was restricted in delivering the material for commercial end use in the United States "to no more than 10 percent of the uranium transferred under this subsection or more than 4,000,000 pounds, whichever is less, in any calendar year after 1997."[11]

The Privatization Act went on to restrict commercial sales of DOE's remaining stockpiles. Such sales were limited to those determined by the Secretary that *will not have an adverse impact on the domestic uranium mining, conversion or enrichment industry.* DOE was further required to take into account in its determination sales of uranium under the Russian HEU Agreement and the Suspension Agreement. Finally, DOE could only sell the government stockpiled uranium at a price that was *not less than the fair market value of the material.*[12]

The presence of the USEC transfer provisions in the Act described above establish that Congress intended that the sales provisions of subsection (d) would apply principally to sales of uranium to parties other than USEC. In fact, the legislative history of the Act indicates that "[t]o enhance the competitiveness of the enrichment market, it is the intent of Congress that the Secretary shall sell material directly into the market in lots of a size that end users can bid on it."[13] This establishes that Congress envisioned sales directly to end users such as electric utilities rather than sole-source sales to USEC. This was critical to domestic producers because USEC has tied sales of uranium with sales of enrichment services. USEC is the only domestic provider of uranium enrichment services and controls through prior U.S. government contracts the majority of U.S. enrichment supply for several more years. Thus, USEC already wields enormous power over consumers of enriched uranium. USEC's tying of sales of uranium with sales of enrichment services enhances its ability to increase its presence in the uranium services market, and also allows it to dominate the market for sales of uranium as they have apparently chosen to do.

While the domestic producers continue to support a strong domestic enrichment industry, we do not believe that subsidizing enrichment sales with transferred U.S. government owned inventories is fair or consistent with the principals in the privatization legislation.

USEC INVENTORY / DOE TRANSFERS TO USEC

In addition to the authorized DOE transfer of approximately 30 million pounds mentioned above, USEC disclosed in its Prospectus that it held additional inven-

[9] See 42 U.S.C. § 2997h-10(c).
[10] S. Rep. 104-173, November 17, 1995.
[11] See 42 U.S.C. § 2297h-10(c)(2)(B).
[12] See 42 U.S.C. § 2297h-10(d)(2).
[13] S. Rep. 104-173, dated November 17, 1995 at 28.

tories at March 31, 1998 totaling about 31.5 million pounds. The revelation of this large inventory came as a complete surprise to the industry and was clearly not contemplated by the sponsors of the Privatization Act.

In addition to this 31.5 million pounds, on May 18, 1998 the Secretary of Energy issued a Determination (Secretarial Determination) which authorized the transfer from U.S. government stockpiles of 3,800 metric tons of natural uranium and 45 metric tons of low-enriched uranium to USEC.[14] USEC also transferred .8 metric tons of HEU at this time. The action of transferring the equivalent of 11.6 million pounds of DOE uranium to USEC violated the restrictions contained in the Privatization Act on the amounts of uranium that could be transferred by DOE to USEC.[15]

To support this transfer, DOE prepared a Secretarial Determination. It is worth noting that the Secretarial Determination and accompanying analysis of potential market impacts characterized the transaction as a *transfer* of uranium rather than a sale. Even if this transaction was a sale, the only discussion of whether DOE received any value for this transfer over and above the transfer set forth in the Act, is a passing reference at page 2 of the DOE Analysis which stated that the transfer is "to settle certain Departmental liabilities at the gaseous diffusion plants." The DOE Analysis offered no explanation of the nature and dollar amount of any such liabilities and whether the settlement of them was intended to represent the fair market value of the transferred uranium. The Secretarial Determination is devoid of any finding that the price paid to the Secretary was the fair market value of the government's material.

More importantly, the Secretarial Determination and Analysis of impacts of the transaction on the domestic uranium industry were fatally flawed. For example, in the Analysis, DOE failed to consider the cumulative effect of the significant quantities of uranium that had previously been transferred to USEC, the effects of higher than expected recovery rates from HEU received under the Russian HEU Agreement, and large quantities of uranium that USEC amassed through underfeeding in the enrichment process.[16]

DOE's Analysis also compared the material transferred with total domestic utility requirements instead of comparing the transaction material to the uncommitted demand of these utilities. DOE's analysis greatly favored a low impact result as it ignored what utilities had already purchased for future deliveries. The volume transferred should have been compared to the uncommitted supply available for a fair and meaningful analysis.

The domestic uranium industry, although the subject of this Determination, was given no opportunity to comment and point out the flaws in the Determination. In fact, the transaction took the industry and the privatization sponsors by surprise. DOE's failure to allow comments was somewhat surprising as the Senate Energy Committee staff had stated in a memorandum, "After the date of privatization, S. 755 allows DOE to market enriched uranium by competitive bid after DOE certifies *(through a full rulemaking process with public comment)* that the sale of the material will not have adverse impact on the domestic mining or enrichment facilities."[17]

DOE's 1998 determination of no adverse impact caused by the entry of 11.6 million pounds is particularly puzzling due to the fact that in 1997 DOE reduced the amount of uranium it was to sell pursuant to a 1997 Secretarial Determination from 3.2 million pounds to one million pounds in recognition of the producing industries warnings of the adverse impacts the sale of 3.2 million pounds would cause. Further, DOE canceled future sales due to changing market conditions that magnified the adverse impacts to the production industry. Certainly nothing changed to lessen impacts of the sales of government transferred uranium between the time DOE canceled its 1997 and beyond sales and redirected their uranium to USEC.

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[14] The Secretarial Determination did provide some protections, stating: "In order to mitigate potential adverse impacts on industry, the Department will restrict the United States Enrichment Corporation's sale of the transferred uranium to a maximum of 35 percent of the total in any single year, with the total quantity to be sold over a minimum of 4 years." However, these restrictions were over and above those established by the Privatization Act. Further, USEC's other uranium inventories were not subjected to these restrictions. Finally, DOE put no enforcement provisions in place to monitor USEC inventory sales of any kind.

[15] See 42 USC § 2297 h-10(a).

[16] Underfeeding refers to a process that uses more electricity and less uranium to attain the desired enrichment, which results in a buildup of excess uranium inventory. When the electricity used during the enrichment is government funded, the net result is windfall of surplus uranium to USEC. EPACT had urged the government enrichment corporation to overfeed, that is, more uranium to boost the market. However, underfeeding proved to be USEC's choice in order to build up its uranium inventory.

[17] June 19, 1995 memo from David Garmen and Sam Fowler to Members and Legislative Assistants, Committee on Energy and Natural Resources.

Again, the revelation that much larger uranium inventories would be transferred to USEC first surfaced publicly in USEC's S-1 Privatization Statement.[18] After reviewing the initial surprise disclosures of USEC's unexpected uranium inventory largesse, Senator Domenici (a key privatization supporter) expressed strong concern over the impacts on the additional transfers on the uranium market.[19] Senator Domenici also expressed grave reservations about the inventory impacts on the Russian HEU Agreement. Senator Domenici felt this was a national security concern and implored the National Security Council to review the impact of the transfer prior to the Administration's decision to approving the sale of the Enrichment Corporation.[20] The announcement of DOE's additional transfers had an almost immediate adverse impact on the uranium market and the domestic industry.

An initial response to USEC's revelation of its expanded inventory holdings and its intent to bring these substantial inventories to the market was the prediction of a major drop in prices by one of the leading industry consulting companies. The Uranium Exchange Company's (Ux) "Market Impact of USEC Inventory Sales" published in July 1998, predicted if, as advertised in the S-1, USEC sold 60 million pounds of those inventories into the market by the end of 2005, the spot market price of uranium would decline to $8 to $10 from 1999 to 2004.[21] If USEC utilized "underfeeding" as they apparently have, the price according to Ux's projection could drop to $6.00 to $9.00 from 1999 to 2004. Ux may have been a bit too pessimistic with their price projection but it appears they did not project that Russian HEU feed would be squeezed out of the market to the extent it has been.

In addition to the damage done to the domestic uranium industry as a result of USEC's uranium, the U.S. Treasury has also paid a big price. Only three months after USEC's privatization, Congress was required to bail out the Russian HEU Agreement by purchasing the natural feed component of the Russian HEU material delivered in 1997 and 1998. An appropriation of $325 million was required to make this purchase. DOE, in recognition of the adverse impacts of its USEC transfers, put this purchase material and its remaining uranium inventories on hold for a ten-year period in an effort to bring some order to the commercial market. While it would be difficult to perceive how the sale of additional DOE material could survive a Secretarial Determination, DOE's action has not had an effect in correcting price imbalances.

In fact, every U.S. uranium producer has curtailed its uranium production since USEC's privatization. Many producers have placed their operations on standby, while others have cut back on production. New Mexico, the historic leader of domestic production, is producing no uranium for the first time since 1955. Many foreign producers have also reduced production as production costs, in most if not all instances, exceed the market price of uranium.[22] It has been devastating to our industry that quantities of uranium beyond those specified in the Privatization Act were transferred and that the Act's four million pounds U_3O_8 per year sales limit has been ignored.

In retrospect, it was a serious mistake to have transferred any U.S. government-owned inventories to USEC beyond a necessary in-process working inventory. The success of the HEU Agreement and an entire industry are now at stake. The result of the excessive government transfers has been production curtailments, mine closures, the termination of development plans, the departure of critical talent, and a total cessation of exploration by every uranium mining company in the U.S. and most overseas companies.

U.S. utilities generally contract two to five years in advance of their actual uranium delivery requirements, leaving some flexibility in their contracts for spot purchases if the spot market is attractive enough. Overseas utilities generally contract even further into the future. Therefore, when USEC was privatized with a large uranium inventory, in order to convert that inventory to cash, USEC was forced to sell at deep discounts into a market already largely committed. This has suppressed

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[18] At page 7 of USEC's S-1, USEC championed its ability to complete sales from national uranium inventory. USEC announced it was "positioned to supplement its uranium enrichment revenues through new sales of natural uranium. USEC's existing inventory contains a substantial amount of natural uranium, which has been supplemented by the transfer of additional uranium from the U.S. Government."

[19] See Exhibit 5 (Domenici to Berger letter of June 26, 1998).

[20] Senator Domenici's concerns were well placed as the U.S. government was forced to pay $325 million in 1998 for the Russian natural uranium components made in 1997 and 1998 deliveries pursuant to the Russian HEU Agreement. See Exhibit 6 (Domenici letter to Frueth, et al. of July 20, 1998).

[21] This compares to UX's projection of $11 to $13 without the addition of USEC's extra material.

[22] See Exhibit 7.

the price of natural uranium obtained by real producers and has devalued the uranium component of the Russian HEU material.

When President Clinton signed the Privatization Act in April 1996, the published uranium price was $16.15 per pound U_3O_8. Since that time, it has dropped to $9.10 per pound U_3O_8. Domestic production in 1996 totaled 6.3 million pounds. This year, production will be approximately 3 million pounds. Perhaps even a better measure of what the USEC Privatization has meant to our industry is reflected in the CAMECO (the largest publicly traded uranium company) share price which has declined from $72.90 in April 1996 to $16.80 at last week's close of the Toronto Exchange—a loss of approximately 80 percent of its value before the USEC privatization.[23]

If nothing is done to correct this situation, our nation will lose valuable mining operations, ore resources and the skilled operators that can produce uranium at very reasonable prices. Due in part to NRC bonding and decommissioning requirements, it is extremely difficult and costly to hold uranium mines in a standby mode.

In 1999, uranium provided about 23 percent of the electric power in the United States. More capital is invested in nuclear generation facilities than all other generating plants combined. In the U.S., only coal fuels more electricity supply, and in Europe and Japan, nuclear power ranks first in electricity production. Because of its low fuel cost, reliability, air quality benefits and secure supply lines, uranium has now become a fundamental energy source in the industrialized world. Yet, it seems that in the United States, some policy makers have come to view the nuclear power industry as a way to absorb surplus military stockpiles of uranium over the short-run rather than as a key power source for the long-run.

The uranium industry can relinquish a substantial share of the commercial market to Russian uranium as provided by the HEU Agreements and the Privatization Act and still maintain a reasonable level of production to maintain competitiveness. However, it cannot survive the uncontrolled dumping of transferred U.S. government stockpiles by USEC.

Mr. Chairman, we urge this Committee to look into why the quantities of uranium to be transferred from DOE to USEC increased from the time the initial privatization plans were agreed to in 1995 and the actual public offering in 1998.

We urge the Committee to inquire as to whether DOE's economic impact analysis of the USEC privatization that determined "no adverse impact on the domestic uranium industry" presumed that the four million pounds U_3O_8 per year USEC sales restriction would be adhered to.

We urge the Committee to consider legislation to clarify the intent of the Privatization Act with respect to uranium transfers and sales and also whether USEC should continue to be granted legal immunity from taking action contrary to the provisions of the Act.

We believe legislation should be adopted to make clear that further transfers of uranium from DOE to USEC would only be authorized after a full hearing from all affected parties and that U.S. government contracts intended to subsidize USEC operations such as low-cost power supply deals with TVA, be evaluated as to their impact on uranium markets and the HEU Agreements.

The domestic producers have met with DOE and other members of the front end of the nuclear fuel cycle to discuss potential remedies to the current situation. In November 1999, the uranium and conversion producers proposed that DOE repurchase the uranium transferred to USEC during the privatization process.[24] This proposal allowed DOE to sell the repurchased uranium when uncommitted demand expanded. This would have allowed DOE to recapture its expenditure and recognize a positive return in the future.[25]

While DOE recognized "that many issues intersect at the juncture of the domestic uranium market—including the continued success of the U.S./Russian agreement on highly enriched uranium," DOE was unwilling to pursue this proposal.[26] DOE did, however, agree to work with industry and other stakeholders to resolve the complex issues raised. We eagerly await any initiatives DOE might put forward. These initiatives may require U.S. taxpayer involvement in financing the Russian HEU Agreement or possibly a tax credit for nuclear utilities purchasing new mined uranium, conversion and enrichment services. We believe a solution can be achieved with Congress' assistance.

Mr. Chairman, it is my fervent hope that we will look back at this hearing as a milestone in refocusing the Congress and the Administration in correcting past

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[23] See Exhibit 8.
[24] See Exhibit 9 (Stout letter to Richardson dated November 24, 1999).
[25] See Exhibit 10 (Rate of Return on DOE Repurchase).
[26] See Exhibit 11 (Magwood letter to Stout dated February 16, 2000).

missteps in the handling of issues affecting the front end of the nuclear fuel cycle. We believe that nuclear power will play a vital role in producing clean, efficient electrical power for our nation, lessening our dependence on coal and foreign oil. The domestic uranium industry, given a level playing field, can compete economically with producers in the western world and assist in maintaining a secure source of fuel for our nation's nuclear power plants. We also need strong conversion and enrichment programs to complete the nuclear fuel cycle. It is of the utmost importance that Congress takes the lead in correcting the errors of the past, and we look forward to working with you and others that recognize the need to do this.

Exhibit 1

A. EPACT

1. **§ 2296b-2. Sale of remaining DOE inventories**

The Secretary, after making the transfer required under section 2297c-6 of this title, may sell, from time to time, portions of the remaining inventories of raw or low-enriched uranium of the Department that are not necessary to national security needs, to the Corporation, at a fair market price. Sales under this section may be made only if such sales will not have a substantial adverse impact on the domestic uranium mining industry. Proceeds from sales under this subsection shall be deposited into the general fund of the United States Treasury.

(Pub.L. 102-486, Title X, § 1013, Oct. 24, 1992, 106 Stat. 2949.)

2. **§ 2296b-3. Responsibility for the industry**

(a) Continuing Secretarial responsibility

The Secretary shall have a continuing responsibility for the domestic uranium industry to encourage the use of domestic uranium. The Secretary, in fulfilling this responsibility, shall not use any supervisory authority over the Corporation. The Secretary shall report annually to the appropriate committees of Congress on action taken with respect to the domestic uranium industry, including action to promote the export of domestic uranium pursuant to subsection (b) of this section.

(Pub.L. 102-486, Title X, § 1014, Oct. 24, 1992, 106 Stat. 2949.)

B. 1996 Privatization Act

1. § 2297h-10. Uranium transfers and sales

(a) Transfers and sales by the Secretary

The Secretary shall not provide enrichment services or transfer or sell any uranium (including natural uranium concentrates, natural uranium hexafluoride, or enriched uranium in any form) to any person except as consistent with this section.

2. **(c) Transfers to the Corporation**

(1) The Secretary shall transfer to the Corporation without charge up to 50 metric tons of enriched uranium and up to 7,000 metric tons of natural uranium from the Department of Energy's stockpile, subject to the restrictions in subsection (c)(2) of this section.

(2) The Corporation shall not deliver for commercial end use in the United States—

(A) any of the uranium transferred under this subsection before January 1, 1998;

(B) more than 10 percent of the uranium (by uranium hexafluoride equivalent content) transferred under this subsection or more than 4,000,000 pounds, whichever is less, in any calendar year after 1997; or,

(C) more than 800,000 separative work units contained in low-enriched uranium transferred under this subsection in any calendar year.

(d) Inventory sales

(1) In addition to the transfers authorized under subsections (c) and (e) of this section, the Secretary may, from time to time, sell natural and low-enriched uranium (including low-enriched uranium derived from highly enriched uranium) from the Department of Energy's stockpile.

(2) Except as provided in subsections (b), (c), and (e) of this section, no sale or transfer of natural or low-enriched uranium shall be made unless—

(A) the President determines that the material is not necessary for national security needs,

(B) the Secretary determines that the sale of the material will not have an adverse material impact on the domestic uranium mining, conversion, or enrichment industry, taking into account the sales of uranium under the Russian HEU Agreement and the Suspension Agreement, and

(C) the price paid to the Secretary will not be less than the fair market value of the material.

(Pub.L. 104-134, Title III, § 3112, Apr. 26, 1996, 110 Stat. 1321-344.)

Table C-13. Ux Uncovered Uranium Requirements Estimate, 2000-2010
(Quantities in million pounds U_3O_8)

Source	2000	2001	2002	2003	2004	2005	2006	2007	2008	2009	2010
U.S. Utilities	1.5	8.5	14.2	28.4	36.7	46.4	51.0	49.0	49.8	53.4	50.6
Non-U.S. Utilities	2.3	11.8	18.2	24.5	30.3	51.7	61.3	64.6	70.2	72.0	77.1
Total Uncovered	3.8	20.3	32.3	52.9	67.0	98.0	112.3	113.6	120.0	125.3	127.7

Figure C-12. Ux Uncovered Utility Requirements, 2000-2010

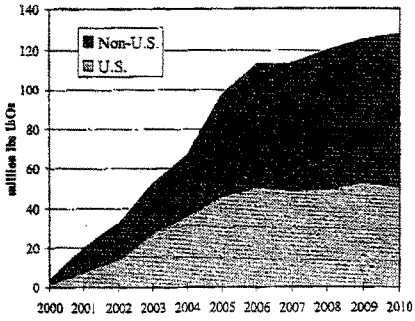


EXHIBIT
2

SUMMARY OF SELECTED URANIUM INDUSTRY PRODUCTIVITIES - 1994

COUNTRY	PRODUCTION CENTER	PRINCIPAL OWNER	PRODUCTION TYPE	PRODUCTION (1000 LBS U308)	EMPLOYEES	PRODUCTIVITY (LBS/EMP/YR)
CANADA	Key Lake	Cameco	conv.	13,190	399	33,058
CANADA	Rabbit Lake	Cameco	conv.	7,456	234	31,863
U.S.	Crow Butte	Uranerz	isl	702	35	20,057
AUSTRALIA	Ranger #1	Energy Resources	conv.	3,223	193	16,699
U.S.	Highland	Power Resources	isl	811	53	15,302
CANADA	Cluff Lake	Cogema	conv.	2,770	250	11,080
U.S.	El Mesquite	Cogema	isl	460	44	10,455
U.S.	Irigaray/Christensen	Cogema	isl	396	46	8,609
CANADA	Stanleigh	Rio Algom	conv.	1,800	275	6,545
NAMIBIA	Rossing	RTZ	conv.	5,000	1,300	3,846
NIGER	Arlit	Cogema	conv.	2,600	830	3,133
FRANCE	Herault	Cogema	conv.	1,352	450	3,004
NIGER	Akouta	Cogema	conv.	5,100	2,132	2,392
GABON	Mounana	Cogema	conv.	1,480	1,000	1,480
SPAIN	Saelices el Chico	ENUSA	conv.	664	703	945
RUSSIA	Krasnokamensk	Priargunsky	conv.	6,000	7,500	800
HUNGARY	Pecs	MEV	conv.	1,074	1,800	597
CZECH	Dolni Rozinka	Diamo	conv.	780	3,000	260
ROMANIA	Feldiora	RAPMR	conv.	300	3,000	100

Notes: Foreign production and employment information obtained from various official and unofficial sources.
U.S. production obtained from the producers or State of Wyoming.
U.S. employment obtained from Mine Safety and Health Administration.

Compiled by: International Nuclear, Inc. - May 10, 1995.

Department of Energy
Washington, DC 20585

The Honorable Craig Thomas
U.S. House of Representatives
Washington, D.C. 20515

Dear Congressman Thomas:

Thank you for your November 21, 1994, letter to Secretary O'Leary regarding the Government-to-Government agreement between the United States and the Russian Federation for the purchase of 500 metric tons of low enriched uranium derived from highly enriched uranium (HEU) removed from nuclear weapons and its effects on the U.S. uranium industry. While the Department of Energy strongly supports recent achievements in Russian nuclear weapons dismantlement and the furtherance of U.S. nuclear nonproliferation objectives, we also share your concern for the viability of the U.S. uranium industry.

The implementation of this agreement, which was signed by the United States and the Russian Federation on January 14, 1994, should be accomplished in a manner that minimizes the impact upon the U.S. uranium industry. It is important to note that the United States Enrichment Corporation, a wholly-owned Government corporation established by the Energy Policy Act of 1992, is the executive agent on behalf of the United States for the implementation of the HEU agreement. It is our understanding that the United States Enrichment Corporation has not purchased any uranium under this agreement. Therefore, no material has been imported into the United States at this time.

In order to ensure that your concerns are properly addressed, I have forwarded a copy of your letter to Mr. William H. Timbers, Chief Executive Officer and President of the United States Enrichment Corporation. The Enrichment Corporation has sole responsibility for placing orders under the agreement with the Russian Federation.

The Department's position regarding the disposition of the material is that the natural uranium component of the purchase agreement should be utilized consistent with public interest provisions of the uranium Antidumping Suspension Agreement and its amendment as negotiated by the U.S. Department of Commerce. This restriction limits the amount of Russian uranium imported for end use in the United States through the year 2003. As a result of this provision the impact on the U.S. uranium industry would be minimal.

Sincerely,

Terry R. Lash, Director
Office of Nuclear Energy

EXHIBIT
4

PETE V. DOMENICI
NEW MEXICO

United States Senate
WASHINGTON, DC 20510-3101

COMMITTEES
BUDGET
APPROPRIATIONS
ENERGY AND NATURAL RESOURCES
INDIAN AFFAIRS
GOVERNMENTAL AFFAIRS

June 26, 1998

The Honorable Sandy Berger
Assistant to the President
for National Security Affairs
The National Security Council
The White House
Washington, D.C.

Dear Sandy:

In recent days, I have become concerned that aspects of the pending sale of the United States Enrichment Corporation; which serves as U.S. Executive Agent for the Russian HEU Agreement, depending upon the way in which that sale is structured, may have a serious impact on implementation of the HEU Agreement and therefore national security. I want to ensure that the National Security Council considers these issues prior to a decision by the Secretary of the Treasury to approve the sale of the Corporation.

The Corporation's inventory of natural uranium may be significantly more than I understood to exist when Congress wrote the USEC Privatization Act. If there is some 30,000,000 pounds more than contemplated in the legislation, the sale of that material would negatively impact the sale of HEU Agreement derived natural uranium and could significantly reduce the Russian Federation's incentive to continue the Agreement. In addition, apparently one of the most recent transfers of material to USEC from the Department of Energy of over 10,000,000 pounds of material to pay for safety upgrades at USEC requires sale into the market at a rate that will exceed the rate stipulated in the 1996 Act, when combined with the sale of the already known material of USEC.

I worry that USEC's future enrichment contracts are not at the volumes or prices anticipated when the decision was made to leave HEU Agreement Executive Agency with the Corporation. As a result, I am not certain that a privatized executive agent can still function in the ways necessary to carry out the national security objectives of the HEU Agreement. As the profit margin on the material from Russia declines (due to the reduced prices USEC is receiving for enrichment services) and this Agreement derived material is becoming a larger portion of the USEC's total sales (due to increased purchases from Russia and decreasing total sales) I wonder if a privatized USEC will be able to sustain this commerce.

EXHIBIT
5

DISTRIBUTED

The Honorable Sandy Berger
June 26, 1998

I have worked for over a decade to privatize the USEC. But if circumstances are different from what we have assumed, you need to take those new circumstances into account before a decision to privatize is made.

Sincerely,

Pete V. Domenici
United States Senator

PS Thanks for all you are doing
PVD

cc: Secretary Rubin, Treasury
Leon Fuerth, OVP
Jack Lew, OMB

United States Senate
COMMITTEE ON APPROPRIATIONS
WASHINGTON, DC 20510-6025

July 20, 1998

Secretary Moler
Leon Fuerth
Larry Stein
Jim Steinberg
Josh Gotbaum
The White House
Washington, DC

Dear Madam Secretary and Messrs. Fuerth, Stein, Steinberg, and Gotbaum:

Based on our conversation today, it is clear you understand the seriousness of the issue with regard to whether the inventory of uranium proposed to be sold with the Enrichment Corporation could imperil the HEU Agreement.

If your remedy to the problem is to appropriate funds to underwrite the HEU Agreement, I may, because I so strongly support the objectives of the HEU Agreement, be forced to support your efforts.

However, you would be much wiser to solve the problem by not creating it: reduce the amount of uranium transferred to the Enrichment Corporation before it is sold.

Sincerely,

Pete V. Domenici

PS If the means you would have to recommend the GI. at least.

EXHIBIT
6

SUMMARY OF U.S. PRODUCTION CUTBACKS, DEFERRALS, AND WRITEDOWNS SINCE USEC PRIVATIZATION

Rio Algom Mining Corp.

Rio Algom Limited took approximately a $45 million writedown on the RAMC properties. Rio Algom Mining Corp. has indicated that it plans to decrease production from 1.8 million lbs. U_3O_8 in 1999 to around 1 million lbs. in 2000. RAMC's Wyoming Reynolds Ranch project has been deferred indefinitely pending an improvement in market conditions. RAMC's New Mexico Ambrosia Lake facility will be shut-in beginning in 2000. The Ambrosia Lake Facility produced approximately 250,000 lbs. in 1999.

Cameco/Power Resources, Inc.

In 1998, Power Resources made an announcement that they will keep Crow Butte production in Nebraska at 800,000 lbs. rather than ramp it up to the previously planned 1 million pounds. PRI also announced that its Wyoming Highland production will drop to 900,000 lbs. rather than the planned 1.5 million pounds. PRI continues to operate both facilities below maximum capacity levels.

Uranium Resources

In 1998, Uranium Resources, the only remaining producer in Texas, determined that it would operate Kingsville Dome/Rosita at minimum levels necessary to fill their sales commitments. After meeting their contractual requirements, URI shut-in their operations in the first quarter of 1999. The company also took an $18 million pretax writedown of the South Texas properties. The company relinquished its rights to the Alta Mesa deposit in Texas.

International Uranium Corp.

IUC, a Utah operator, shut-in its Sunday, GMG, and Rim mines in 1999. Their Topaz mine was also shut in recently.

Cogema, Inc.

Cogema announced plans to cease production at the Wyoming Christensen Ranch/Irigaray sometime during the fourth quarter of 2000.

U.S. Energy

In 1998, U.S. Energy announced that they had suspended development at their Jackpot uranium mine in Wyoming. The reason behind the suspension was directly related to the government's transfers of inventories to USEC. (Ux Weekly – August 3, 1998)

IMC-Agrico

IMC shut down its uranium production as a by-product of phosphate recovery at the Uncle Sam/Faustina located in Lousiana. There are no plans to restart production from these facilities.

Cotter Corporation

Cotter Corporation decided last month to shut in its Schwartzwalder mine located in Colorado.

Impacts of USEC Privatization Act on Uranium Spot Price and Cameco Share Price

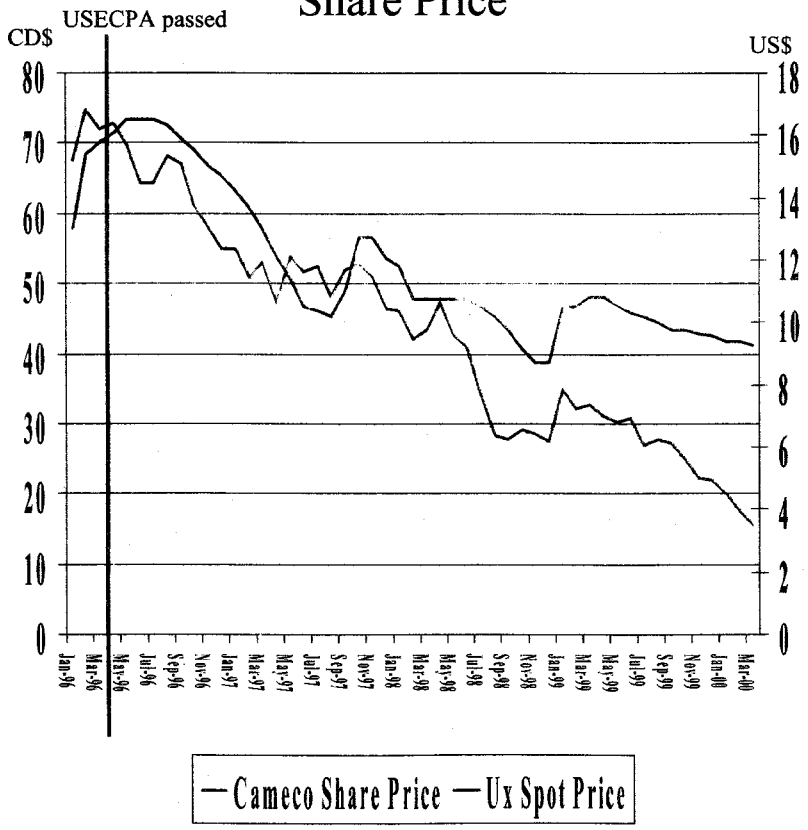


Exhibit 8

Rio Algom Mining Corp.

R. Mark Stout
Vice President, Land & Marketing

November 24, 1999

The Honorable Bill Richardson
Secretary, Department of Energy
1000 Independence Ave., SW
Washington, D.C. 20585

Dear Secretary Richardson:

Members of the domestic uranium mining and conversion industry, represented by the undersigned companies, are facing unbearable economic hardship as a result of the mismanagement of the U.S./Russian HEU Agreement pursuant to the USEC Privatization Act. The transfer of DOE stockpiled uranium to USEC in amounts greater than set forth in the privatization legislation has served to severely undermine the delicate supply/demand balance of the world's uranium market and risks the continued implementation of the HEU Agreement.

All of the previous analyses and negotiations sponsored by the U.S. Government to ensure absorption of HEU derived material into the domestic marketplace without significant injury to the domestic uranium mining industry became irrelevant upon USEC's disclosure of its intended sales of former DOE inventories as set out in their stock prospectus issued on June 29, 1998. As noted in your recent correspondence to USEC, the negative impact of USEC natural uranium sales threatens the foundations of the HEU Agreements.

The domestic uranium mining and conversion industry has witnessed the erosion of its market since the first CIS uranium was sold in the U.S. during the late 1980's. We have continually conceded our market position to support important political agendas, especially with respect to the HEU Agreement, the privatization of USEC, and CIS trade issues. Today there is nothing left to concede.

Uncommitted demand by U.S. utilities over the next few years can be met solely by USEC sales of former DOE inventory, to the detriment of domestic producers and the HEU Agreement. As reported in Mr. Timber's letter to you of October 29, 1999, USEC plans to supply, on average, between 6% and 7% of world demand over the next 3 to 4 years. This equates to between 10 and 12 million pounds of uranium (U_3O_8 basis) per year, which represents, in turn, approximately 25% of annual U.S. demand. As USEC and others vie to complete limited sales opportunities, market prices will come under increasing downward pressure. As a direct result, continued implementation of the HEU Agreement will be at risk, and domestic mining and conversion companies will be forced to shutter remaining plant capacity and abandon uranium reserves.

In our view, this combination of U.S. government policies, i.e., (1) the negotiation and implementation of the CIS Suspension Agreements by the Department of Commerce, (2) the HEU Agreement and U.S. sponsorship of the related feed material sales agreement, and (3) the DOE uranium

6305 Waterford Boulevard, Suite 325, Oklahoma City, Oklahoma 73118 • (405) 848-0153 • FAX (405) 848-1208

transfers to USEC, have had a cumulative impact on the uranium market far beyond that intended or considered by the U.S. government policy makers. The combined impact of these policies has been to take the investments made by U.S. producers by assigning all of our market to USEC and to imports of natural and enriched uranium from Russia and the other former Soviet states.

It is imperative that immediate action be formulated to create a solution to these problems. In this regard, we have prepared the following proposal for your consideration:

1. Purchase of USEC inventory: DOE will purchase USEC's uncommitted inventory (assumed to be approximately 50 million pounds U_3O_8 equivalent) at the higher of book value or market price. Delivery/payment will take place over a 3-year period, 2000-2002, which we believe should generate at least $150 million in revenue to USEC in each year.

   Subject to a secretarial determination of no material adverse impact on the domestic uranium industry or the HEU Agreement, beginning in 2003 DOE shall be allowed to sell, by auction, up to 4.0 million pounds of this uranium in each year concurrent with the term of the HEU Agreement. This quantity limitation is consistent with the USEC Privatization Act of 1996 which prohibits USEC from selling more than 4.0 million pounds of uranium transferred from DOE in any calendar year after 1997.

   As part of this transaction perhaps USEC and DOE could agree to a specified period in which USEC would commit to operate both GDP facilities and remain as the U.S. executive agent under the HEU Agreement.

2. The domestic uranium mining industry will withdraw its suit against DOE (*Power Resources, Inc., et al. v. DOE*, Civil Action No. 98CV177) challenging uranium transfers to USEC, upon the establishment/execution of a purchase agreement between DOE and USEC regarding the uncommitted balance of USEC inventory as outlined above.

The above proposal will serve to remove the current market uncertainty facing all industry participants. By removing an apparent desperate seller of uranium from the market, we expect the resulting DOE inventory to increase in value as market prices recover. We look forward to your reply and would be pleased to discuss this proposal in greater detail with you at your earliest convenience.

This proposal letter is being signed by R. Mark Stout on behalf of and with the prior authorization of each of the companies listed below.

Very truly yours,

R. Mark Stout, Vice President, Land & Marketing
Rio Algom Mining Corp.
Suite 325
6305 Waterford Blvd.
Oklahoma City, OK 73118-1119

Earl Hoellen, President and Chief Executive Officer
International Uranium Corporation
Suite 950
Independence Plaza
1050 Seventeenth Street
Denver, CO 80265

Joe H. Card, Senior Vice President
Uranium Resources, Inc.
South Building, Suite 2
5180 Roswell Road NW
Atlanta, Georgia 30342

Rich Ziegler, Executive Vice President & General Manager
Cotter Corporation
Suite 350
12596 W. Bayaud Ave.
Lakewood, CO 80228

Keith Larsen, President
U.S. Energy Corp.
877 N. 8th Street
Riverton, WY 82501

Jim Graham, President
ConverDyn
Suite 600
5000 South Quebec Street
Denver, CO 80237

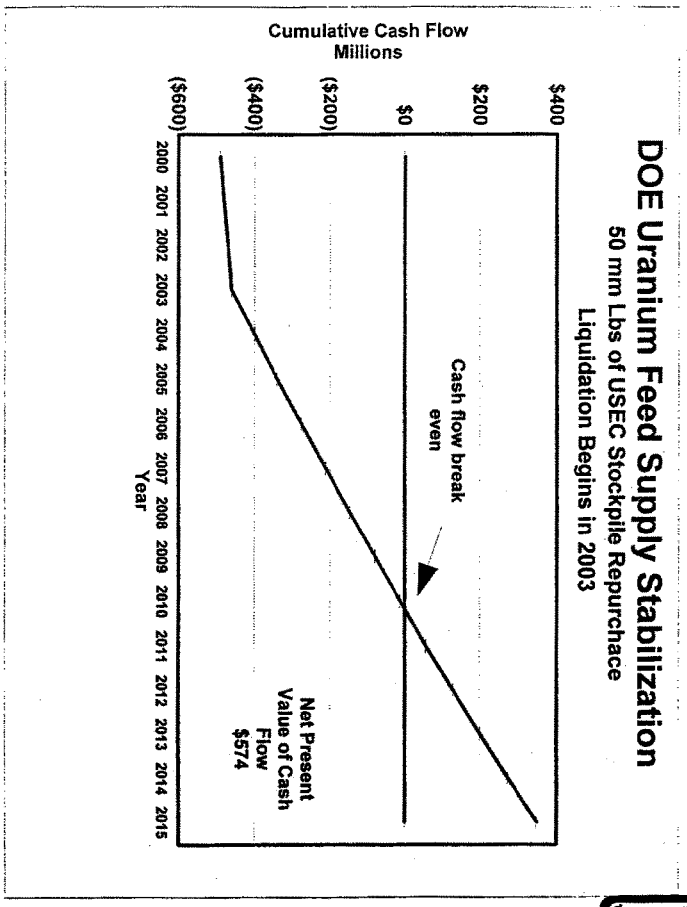

DOE Uranium Feed Supply Stabilization
50 mm Lbs of USEC Stockpile Repurchase
Liquidation Begins in 2003
Cumulative Cash Flow
Millions
$400
$200
$0
($200)
($400)
($600)
Cash flow break
even
Net Present
Value of Cash
Flow
$574
2000 2001 2002 2003 2004 2005 2006 2007 2008 2009 2010 2011 2012 2013 2014 2015
Year


EXHIBIT
19

Department of Energy
Washington, DC 20585

February 16, 2000

Mr. R. Mark Stout
Vice President, Land and Marketing
Rio Algom Mining Corporation
6305 Waterford Boulevard, Suite 325
Oklahoma City, Oklahoma 73118

Dear Mr. Stout:

Thank you for your letter of November 24, 1999, to Secretary Richardson regarding uranium market conditions, issues, and your proposal designed to remove market uncertainties facing the industry today.

I appreciate you, Mr. Indall, Mr. Pelizza, and Mr. Byers meeting with us in Washington on January 20, 2000, to review the state of the domestic uranium industry and your proposal. The meeting was very enlightening and helpful in understanding the concerns of the uranium industry and your suggestions regarding actions the Government should take to enhance the viability of our domestic uranium producing industry. While, as we discussed, the Department of Energy does not currently possess the resources to implement your ideas, we continue to discuss your suggestions within the Government.

We recognize that many important issues intersect at the juncture of the domestic uranium market - including the continued success of the U.S./Russia agreement on highly enriched uranium, which is very important to our national security objectives. We will continue to work with industry and other stakeholders to resolve the complex issues raised during our meeting. Please do not hesitate to contact us as we continue to consider options to address these challenges.

Sincerely,

William D. Magwood, IV, Director
Office of Nuclear Energy, Science
and Technology

Mr. WHITFIELD. Thank you, Mr. Stout.

We have been called for our last vote of the day, but I would like to go on with Dr. Brewer and get your opening statement.

TESTIMONY OF SHELBY T. BREWER

Mr. BREWER. Thank you, Mr. Chairman. I am pleased to be here to give you whatever perspective I can on this situation. As you know, I had—I have had less than 1 week to prepare. About 17 years ago, I was in the Reagan administration during the first term; and I had responsibility for all of the nuclear activities in the Department except weapons production. Uranium enrichment was one of the responsibilities, and we had a very severe market crisis during my tenure there. We took very acute and realistic actions to turn that situation around and got the market back. We reduced cost. We reformed the contract format. We made provisions to burn out the secondary market which was being fed by overpricing and take-or-pay contracts, et cetera; and I emerged from that near-death experience with a conviction that we needed to run this business like a business.

Now 17 years later and 2 years after the celebrated IPO, the ox is in the ditch and you know the statistics. They have been cited several times today. The stock value has depressed 70 percent. Market cap is down to $400 million. The company has lost its credit standing, credit rating. Market share is down. Costs are up. Backlog is down and most important, the quality of the backlog, the margin implicit in the backlog is not there. It is gone. And so—and reported earnings and projected earnings are down. Moreover, USEC is selling their inventory, $1 billion worth of inventory roughly that they inherited from the Department of Energy. They are selling it rapidly to cover these operating deficits. You have just heard that.

This raises a very crucial issue in my mind. What did USEC management know in 1998 at the time of the IPO that is now known? I should have said what did they not know then that is obvious now. It was obvious then. It was obvious 5 or 6 years ago that there was an elephant in the living room, and it is just that simple. Now you have them here on Capitol Hill with this pathetic the "dog ate my lunch"—or "dog ate my homework" excuse. It was the market that did it. It was the Russian deal that trashed them. And it is baloney; it really is. They negotiated the Russian deal. Why would they negotiate something that places them at disadvantage?

So I would like to refer—and I will be very brief. As Henry the IV said to his wives, I won't keep you long—to the figure in my testimony and I will make these points very briefly. They are selling below their total cost of production plus margin. And that can't go on indefinitely. Their proposal now is to renegotiate the Russian contract. Well, they can add maybe—they can reduce their cost by maybe $5 an SWU, not much to write home about.

There are—the other proposal that is being discussed is the shutdown of a GDP, either Portsmouth or Paducah. That too is only a temporary Band-Aid because Avlis has been terminated. Avlis has been terminated. If you look at my chart, Mr. Chairman, they are back in the soup even with the termination of a GDP in the year

2004. And that is because the negative backlog or the nonquality backlog in their order books keeps growing on. It is a gift that keeps on giving year after year after year. So I wish I could be more responsive to your invitation for finding a magic bullet that would fix all of this and in 1 week's time I have not done that.

But I know that blaming the Russian deal is a red herring. That is not it. The way they are contracting for SWU production now is not it. The backlog that they inherited was $125 an SWU which is—or the contracts I signed in the early 1980's. And then of course as has been discussed today and I won't go into it, the IPO process itself is suspect. With the borrowing of half a billion dollars in order to trump the bid of a private company to acquire USEC, where was the SEC and the Treasury during this oversight, during this process? I will quit at that point. I think I am in enough trouble.

[The prepared statement of Shelby T. Brewer follows:]

PREPARED STATEMENT OF SHELBY T. BREWER, S. BREWER ENTERPRISES, INC.

Mr. Chairman and members of the Committee, I wish I could say that I am pleased to present testimony on this subject. The Uranium Enrichment Enterprise was one of my responsibilities when I was in the Reagan Administration in the early 1980s. We faced a severe market crisis in those days, and were able to turn it around and save the business from insolvency. We owe much of the credit to John Longnecker who I appointed to head the enrichment enterprise. The business emerged stronger because we took painful actions to reduce costs, became more customer attentive. We slimmed down, shaped the business, and became competitive. John and I emerged from this "near death experience" with the conviction that the Uranium Enrichment Enterprise urgently needed to be fundamentally restructured and run like a business, market-driven, rather than an instrument of U.S. foreign policy, a contractor feeding trough, and as a federal cash cow, an irresistible plaything for federal budget aficionados barnacling onto any available revenue stream. John and I strongly supported the government corporation element of the 1992 Energy Policy Act.

The financial performance of the privatized entity, United States Enrichment Corporation (USEC), has been dismal, and it's future looks grave. I cite the following indicators:

1. The stock price has fallen by more than 70%, reducing USEC market capitalization from $1.6 Billion in 1998 to about $400 million in early year 2000.
2. Standard and Poors downgraded its credit rating at the end of August 1999, and again in February 2000 to below investment grade, with a future outlook as "negative".
3. On February 23, 2000, Moody's also downgraded USEC's senior unsecured bank credit and short-term debt ratings.
4. Merrill Lynch, one of the IPO underwriters, downgraded USEC's stock in February 2000 based on concerns regarding future cost compositeness.
5. USEC slashed its dividend in February 2000 due to poor financial performance.
6. Fiscal year 1999 sales were less than promised, and fiscal year 2000 revenue estimates were lowered by about $100 million.
7. Despite aggressive sales of uranium inventories (transferred from the Department of Energy to USEC), fiscal year 2001 earnings estimates have been lowered to about $35 Million. USEC's annual report for 1999 noted that net income has fallen consistently. Selling this inventory is like living on principal rather than earnings.
8. Gaseous Diffusion Plant (GDP) production costs increased and exceeded $95/SWU, in contrast to USEC's goal of achieving GDP production costs of $75/SWU.
9. USEC market share both world and US has declined: the US market share has declined from 90% to 75%, and the world market share has declined from 70% to about 40%. The backlog has declined, and the quality of the backlog (margin) has declined drastically as USEC began contracting SWU deliveries below cost.

What concerns me most is the trend toward an ultimate liquidity (cash flow) problem, a short step away from bankruptcy. I have no access to USEC internal data, and properly so. I am using only data which is in the public domain, and have had

less than one week since the invitation to testify, to data-gather and analyze. In recent trade press interviews, USEC's senior management has discussed USEC's declining revenue and increasing costs.

Using USEC's method of comparison, my projection of USEC's financial condition (based on its SEC filing) is quite daunting as shown in the attached figure. Terminology in the figure is defined as follows:

USEC Breakeven Cost is the sum of direct GDP production cost, plus Sales, General and Administrative Expenses (SG&A), plus Research Development, plus Dividends. This is the price that would recover all Production costs, overhead costs, and return a profit margin.

GDP Cost is the sum of Power Purchase Cost, plus Depreciation, plus Maintenance and Other Operating Costs.

Average Sales Price is the Revenue divided by SWU production.

The figure is intended to show fundamental concepts and trends. Data has been taken from public domain sources, since I do not have access to USEC's internal books. One can argue about the absolute magnitudes and the dates in the figure, but the point is to illustrate trends and prospects.

Several points can me made from the figure.

1. First, Average Sales Price in the immediate future drops below USEC Breakeven Cost, that is, the price the actual price is insufficient to cover costs and provide a return to the stockholders.

2. This condition persists until about 2003, when USEC when USEC Breakeven crosses under the Average Sales Price.

3. This assumes that (a) the Soviet deal is renegotiated to trim about $10/SWU off the Soviet price (a net savings to the enterprise of about $5/SWU); (b) one GDP is closed (about 2002).

4. Beyond about 2004, Average Sales Price falls below USEC Breakeven again, so that the Soviet renegotiation and the GDP shutdown are not permanent fixes as long as USEC continues to contract product sales under cost. Recent sales prices are just about $80/SWU, and impact of these sales roll out into the future.

Again, I do not want to imply that this chart is based on rocket-science analysis. It is intended to define the crisis, show major trend lines, and to roughly measure impacts of remedies which have been discussed.

From the analysis summarized in the figure, believe, *I believe that USEC will continue to experience significant financial problems, namely losses from its core business that USEC-management will try to offset by selling inventories inherited from DOE, a non-viable and non-substantive stratagem for the short or long term.*

One (of the several) excuses that USEC management has made for its poor performance is the that the uranium purchase deal with the Russians, for National Security and diplomatic purposes, injures USEC'S bottom line. This is a red herring. First of all, the Soviet Union deal was negotiated in by USEC itself as the executive agent of the US Government. They negotiated a deal which they are now complaining about. Second, the classical "make or buy" mathematics was applicable in the early 1990s when Soviet quantities were small and the marginal cost of U.S. production was significantly lower than it is now. In that time frame, there was indeed a penalty for buying the Soviet material. Now, however, the quantities to be purchased from the Soviets will account for almost half of the total USEC SWU deliveries, and the cost of producing this material internally at the US GDP's is significantly above the Soviet price. This is because new, firm power, power purchase agreements will have to be negotiated, probably significantly above the roughly 2 c/kwh price USEC now pays. The price for purchased power could be as high as 3 c/kwh. In short, the purchase of the Soviet material is a plus, not a negative, to USEC's bottom line. Third, the transfer of the DOE stockpile, valued at about $1 Billion, offset any disadvantage the Soviet deal imposed on USEC in early days of implementing the deal. For USEC to come to Capital Hill with a tin cup, pleading for a subsidy, is disingenuous. The Soviet deal cannot be used as a crutch to excuse poor management.

USEC will argue that all of the maladies their business suffers were and are beyond their control. I disagree. Apparently not understanding that it was in an oversupplied, buyers-market, USEC did not adopt a competitive price ceiling once the Atomic Energy Act Section 161v evaporated in 1992. Over the side went my and John Longnecker's pledges to reduce costs/prices further below the $125/SWU we contracted for in the early 1980s. As a result of this gouging, USEC lost market share, and actually sued its customers for terminating contracts and seeking other supply options. When this strategy proved ineffective, USEC began selling SWUs under its current cost. The customer population regards USEC as a very unstable source of supply, and this perception results from the arrogance and ineptitude of the company.

Another critical question is the foundation of the Initial Public Offering (IPO) process itself, and the representations made at the time. It is clear to me that the enterprise was hugely overvalued in garnering in excess of $1.5 Billion in stock placement. For one thing, the uranium stockpile inheritance (evaluated at about $1 Billion) was a gross overstatement, in that this is not immediately fungible. If one tried to convert this to dollars rapidly, the market price would collapse. The correct way to evaluate the stockpile is to compute the present value of a long Stream of modest stockpile sales, using classical discounted cash flow methods. The selling would stop when the inventory level reached that working inventory needed to run the business efficiently Another issue with the EPO process is the curious loan of $500 Million that USEC management obtained to trump the bid of a private company to acquire USEC. The industry knew of course that the last thing that USEC management wanted was a simple straightforward acquisition of the business as a method of privatizing. The transaction was sort of characterized as a hybrid LBO/IPO transaction. Whatever, the debt service on the $500 Million loan is on the backs of the USEC IPO stockholders. Where was Federal (Treasury and SEC) oversight during this process?

The Treasury and the taxpayer cannot complain, because the money to trump the private company offering was obtained and deposited in the Treasury. What makes it public business now, however, is that USEC is seeking a federal subsidy, and because the future of U.S. uranium enrichment capacity is a national security issue. Therefore, Mr. Chairman, your oversight is timely.

Subsidizing this failed business and its management is not a solution, but another invitation to further industry cynicism, by rewarding sloppy and inept commercial practice.

Since I received the invitation less than one week ago to be here I have thought long and hard about an equitable solution for the U.S. Government, the USEC stockholders, and an operational fix to the financial meltdown we see in USEC. I am sorry that I cannot present to you a surgical failsafe recommendation at this time, a set of silver bullets.

The first set of recommendations are peripheral, obvious, hard, and do not solve the endemic problem.

(a) renegotiate the prices paid to the Soviets—this is the USEC proposition, and I wish them well, although they negotiated the current Soviet scenario and have little credibility. Also, from the Figure, the potential improvement on the USEC bottom line (about $5/SWU), is not large.

(b) close one of the two GDPs, and try to make significant savings in operating and maintenance expenses—this could significantly improve USEC's bottom line, but would not be a lasting solution, as USEC's poor quality backlog will continue to flow through (prices below cost) the books.

(c) negotiate new power supply contracts—I doubt if this would reduce power price—in all likelihood, the price would increase;

(d) advise USEC to enter new adjacent businesses, to diversify—However, USEC has no cash or credit-worthiness to make acquisitions, and the management team is not credible, so this approach is not viable.

None of the above nibbling-at-the edges approaches have a high success probability, enough to offset the financial disaster, nor could they arrive in time to save the enterprise. Therefore, deep and major structural changes are in order. I am totally opposed to subsidizing USEC from the tax base. (If anything, USEC should pay back a portion of the advantage it enjoys from the Soviet windfall.)

Therefore I believe major structural changes must be contemplated, and that will involve legislation. These are my thoughts:

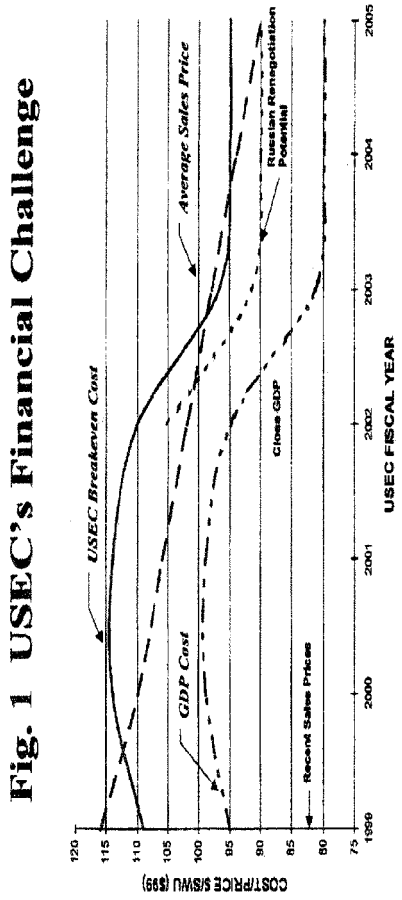
A) First, separate and delineate clearly and budget separately roles of national security/diplomacy from USEC.

B) Have the Departments of Defense or Energy reclaim beneficial control over one GDP for national security purposes. The plant could be put in a hot standby configuration if there is no near-term need for HEU production. If there is a payment owed to USEC stockholders, make it.

C) Compute mathematically any loss of USEC stockholder value due to the Soviet deal as it was implemented when marginal costs of production were less than the Soviet price, less any gain from the Soviet deal more recently (when USEC's production costs have increased significantly).

D) Encourage USEC stockholders to examine creatively the prospect of a merger or divestment with another enrichment supplier, or successful adjacent operator in the nuclear fuel cycle.

Mr. Chairman, I wish I could be more optimistic, and more helpful to the Committee. I wish I had more definitive recommendations as to a solution. Thank you for the invitation to be here.



Mr. WHITFIELD. We will recess for about 10 minutes; and then we will come back, Dr. Stiglitz, and have your testimony and Mr. Miller's. I apologize for this delay, but it won't be very long.

[Brief recess.]

Mr. WHITFIELD. I would like to reconvene the hearing and Dr. Brewer had just finished his testimony. So, Dr. Stiglitz, if you would give us your testimony.

TESTIMONY OF JOSEPH E. STIGLITZ

Mr. STIGLITZ. Thank you. It is a pleasure for me to appear before you to testify on this subject of the privatization of the U.S. Enrichment Corporation. As I point out in my written testimony, from 1993 through 1997 I served as a member and chairman of the President's Council of Economic Advisors. In that capacity I participated in extensive discussions on the privatization issue. In my years on the council, I faced a large number of complicated and technical issues in which there was considerable uncertainty about the merits of alternative courses of actions. Decisions had to be made and these decisions entailed difficult judgment calls. The privatization of USEC was different. This was an issue where there were serious large down-side risks and virtually no upside gains. What I want to do is describe what I thought of as the central down-side risks and what are the alleged benefits and why I thought they were so minuscule.

The main basis of our opposition was really one that went to the issue of nuclear nonproliferation. And as economists, the reason that we were involved is that we had to assess what the incentives of USEC as a privatized entity would be. There had been this important agreement that has been referred to a number of in—a number of times where we were bringing in the HEU from Russia. I think all of us believed very strongly this was a bipartisan Bush-Clinton initiative, getting as much of that into the United States as fast as possible. So we thought that was very important; and as economists we then had to ask the question if it were privatized, would there—what would their incentives be. We came to the very strong conclusion that it was not—it would not be in their interest as a privatized entity to maintain that flow of HEU and that they would engage in one way or another a variety of ways of trying to do everything they could to stop that flow coming in.

One way of putting it, we argued that there was an inevitable conflict of interest between the interest of the privatized new monopoly in the U.S. and the national interest in seeing that as much of the uranium be brought into the United States as possible. We have seen—even while USEC remained under Timbers within the U.S. Government, we have seen manifestations of the potential conflict of interest and the dissembling to which it could give rise.

When Russia offered to increase its sales substantially, USEC declined the offer and payment could only be interpreted as hush money to keep the agreement secret. Even after the secret agreement was signed, representatives of USEC in a meeting at the old executive office building denied that they would ever engage in activities that would slow down the flow of enriched uranium. They would always put the national interests first and they said it with seeming conviction. But to be sure when they made those strong

denials, they were unaware that there were those at the meeting who already new about the secret agreement that they had already signed or that the council of economic advisors would manage to learn of its contents within days. There were other examples, manifestations of conflicts of interest that I don't have time here to talk about and I didn't in my testimony; but if you want a more extended discussion, I could do that.

At the council, we also addressed the issue of whether there were mechanisms of regulatory oversight that would be able to address effectively the issues of conflict of interest; and we came to the conclusion that that would be very difficult, and some of the discussion earlier today has highlighted some of the difficulties, for instance, oversight on the safety issue and the kind of bind that the government would get into if they failed to meet the regulatory requirements. So we, in fact, had anticipated that; and that had been a source of our concern. Those on the other side said well, don't worry about these things. Regulation oversight will take care of it.

There were other problematic issues associated with privatization, one of them being competition policy. Those in the antitrust division shared our view that this was not an industry that was competitive; and, therefore, normal private market forces were not at play.

The conclusion I just had time to touch on was that there were clear down-side risks, and the question then is were there off-setting benefits. And our belief was strongly that there were not beliefs—there were not benefits to anyone who is not absolutely committed to privatization as an end in itself. Only if you took that as your goal, would privatization be something that you would say is valuable.

The economic benefits, the efficiency gains that had been hoped from privatization, actually there have been enormous gains already in the preceding years through the process of corporationization. So the benefits that one would hope to get from privatization, we do not anticipate any significant further benefits.

Moreover, the standard argument for privatization which is derived from intense competition from private firms were not applicable in this case precisely because this is not a market in which most of the other firms are private. In fact, all of the other firms in the world have a very large public role. And there is actually a high degree of market concentration.

One of the alleged benefits of privatization was that it would provide funding for the new AVLIS technology. We engaged in consultations on this matter and came to the view that the prospects for the new technology were limited at best.

We also came to the view that this was not what you might call a clean privatization. That is to say the government was assuming a whole variety of liabilities not only environmental but the kind that Representative Strickland talked about earlier; and so this is not the kind of usual privatization that you think of where you have a clean transfer of assets to the private sector of a steel mill or something like this. This was an area where there was inherent conflict, inherent important public role that could not be separated from the privatization process.

One of the driving forces for privatization was obtaining the President's commitment to a balanced budget, an issue which seems particularly irrelevant given today's budgetary situation. Things turn around quickly in this world. But as an economist, this argument was especially questionable since privatization revenue shouldn't even be included in the budget since they constitute a sale of an asset. So our view was this was a whole bogus issue. But even if you took it on its face, the fact of it is that if you look at the privatization and how much revenue did the Government get and a point that has already been made, $1.9 billion; but then you ought to subtract out the fact that it was given all this uranium. Anybody can sell uranium. You were talking about selling the corporation. At one time they actually also talked about putting cash reserves. Selling cash is not very difficult either.

The interesting thing, of course, is that there is an incentive to boost up the value of the total enterprise, the corporation including the uranium, because, of course, the commissions that are given are based on the total asset sale—the commission to the companies that do the sale are usually based on asset value. So they include the $1.9 billion, not the $900 million or whatever is the value of the company. So they were getting very large commissions on the sale of uranium, and I am sure anybody else selling uranium would have enjoyed commissions at those levels.

As it turned out, many of the concerns that we raised in the course of the privatization debate seemed unfortunately to have been borne out. The AVLIS technology was abandoned. The revenues raised were not substantial and the budgetary situation clearly made the whole issue barely germane. According to newspaper reports, the privatization at times has put at risk a broad range of negotiations over nuclear proliferation issues.

And again USEC has expressed at times reluctance at continuing the importation of material from Russia. The regulatory issues that we were concerned about have again surfaced in an important way. The national benefits from the privatization have yet to be demonstrated. The risks presented are already all too apparent. And let me just conclude on one remark about the decisionmaking process itself.

I regret that there was not a full, open discussion of the issues prior to privatization. I cannot see how any issue of national security was served by the secrecy and lack of transparency that surrounded so much of the privatization process. Greater openness would have subjected the decision to more intensive public scrutiny, and that scrutiny I believe may well have led to a different outcome, one that I still believe would have been far more in accord with our overall national interests. Thank you.

[The prepared statement of Joseph E. Stiglitz follows:]

PREPARED STATEMENT OF JOSEPH E. STIGLITZ, WORLD BANK

It is a pleasure for me to appear before you to testify on the subject of the privatization of the U.S. Enrichment Corporation (USEC). During the period 1993 through 1997 I served as a member, and then Chairman, of the President's Council of Economic Advisers. In that capacity, I participated in extensive discussions on that issue. In my years on the Council, I faced a large number of complicated and technical issues, in which there was considerable uncertainty about the merits of alternative courses of actions. Decisions have to be made, and these decisions entail hard judgment calls.

The privatization of USEC was different. This was an issue where there were serious, large downside risks, and virtually no upside gains. It was an easy judgment call, one that I came to feel strongly about, and where my judgment was shared by all those in the Council and its staff who looked at the issue. It was a view, by the way, which was also shared by those in the academic community (mainly those involved in national security issues), with whom I discussed the issue.[1] While I was Chairman, we succeeded in presenting the adverse case against privatization sufficiently effectively that it was delayed, but as you all know, shortly into the Administration's second term, the privatization was finalized.

Central to the Council's opposition to privatization was a concern about issues of nuclear non-proliferation. We strongly agreed with the commitment of both the Bush and Clinton Administrations that it was in everyone's interest that as much of the enriched uranium from the nuclear warheads be deenriched and transferred to the United States as quickly as possible, and were highly supportive of the swords-to-ploughshares agreement made with Russia that entailed the de-enriched uranium being use for nuclear power plants. USEC had been assigned the role of the exclusive agent for bringing the material into the United States and marketing the LEU (low enriched uranium) to electric utilities. This made sense, given the dominant market share that the USEC, at the time, a public entity, had, not only in the United States, but around the world. But privatization would change all that. Our analysis showed convincingly and beyond any shadow of a doubt that it would not be in the interests of a privatized USEC to bring the material into the United States; the costs of producing enriched uranium (especially at the low rates—arguably below market—at which USEC obtained electricity) were less than the fair market price at which USEC would be required to purchase the material from Russia. There was an inevitable conflict of interest—between the interests of the privatized near-monopoly in the U.S., and the national interests in seeing that as much of the uranium be brought into the United States as possible.

We had seen manifestations of the potential conflict of interest—and the dissembling to which it could give rise—even while USEC remained within the public sector. When Russia offered to increase its sales substantially, USEC declined the offer and paid what can only be interpreted as hush money to keep the agreement in secret. Even after the secret agreement was signed, representatives of USEC denied, in a meeting at the Old Executive Office Building, that they would ever engage in activities that would slow down the flow of enriched uranium; they would always put the national interests first! To be sure, when they made those strong denials, they were unaware that there were those at the meeting who know about the secret agreement, or that the Council would manage to learn of its contents within days. But this was not the only example of a manifestation of a conflict of interest which I could relate before you today.

An issue that we debated extensively was whether there were forms of regulatory oversight that could adequately address this and other conflicts of interest issues. There was also a debate about whether the threat of terminating USEC's exclusivity in importing the enriched uranium sufficed to ensure "good behavior" on the part of the USEC. Our conclusion was that it was not, nor did we have confidence that an effective regulatory mechanism could be set into place.

There were other problematic issues associated with privatization. For instance, the high level of market share raised concerns about the effectiveness of competition. Given that, had USEC been in the private sector, it is unlikely that an agreement to become the exclusive agent for importing the material from one of the few competing sources would have passed anti-trust scrutiny. My concerns for the anti-competitive effects were shared by those in the anti-trust division of the Department of Justice with whom I spoke.

There were thus clear down-side risks. Were there offsetting benefits? These were not apparent to anyone not absolutely committed to privatization as an end in itself. Major efficiency gains had already been achieved, and it was not apparent that there were significant further efficiency gains to be had from privatization. Moreover, the standard arguments for privatization, derived from intense competition from private firms, were not fully applicable in this case. USEC had a major share of the world market, there were only a few other firms; all of the other firms had substantially public sector ownership; and even if were later to become privatized, governmental interests in maintaining a supply of enriched uranium implied that there might not be the standard arms-length relationship to government. One of the alleged benefits of privatization was that it would provide funding for the new

[1] At a meeting of the Council of Foreign Relations in which the issue was discussed, not a single individual could identify benefits of privatization which were at all commensurate with the risks.

AVLIS technology. We engaged in consultations on this matter, and came to the view that the prospects for the new technology were limited at best.

One of the driving forces for privatization was attaining the President's commitment to a balanced budget—an issue which seems particularly irrelevant given today's budgetary situation. As an economist, this argument was especially questionable, since privatization revenues should not even included in the budget, since they constitute just a sale of an asset. Indeed, while revenues in the year of the sale increase, revenues in subsequent years would decline. The long run impact on the public debt accordingly was likely to be small at best. As it turned out, the net revenue attained from the sale of USEC (net of fees paid for privatization and net of the sale of uranium which accompanied the sale of USEC) were sufficiently small—especially when account is taken of the future lost revenues—to make it clear that the benefit was not at all commensurate with the risks.

As it turned out, many of the concerns that we raised in the course of the privatization debate seem, unfortunately, to have been borne out. The AVLIS technology was abandoned. The revenues raised were not substantial, and the budgetary situation clearly made that whole issue barely germane. According to newspaper reports, the privatization, at least at times, has put at risk a broad range of negotiations over nuclear proliferation issues. And, again, according to newspaper reports, USEC has expressed at times reluctance at continuing the importation of the material from Russia. The national benefits from the privatization have yet to have been demonstrated. The risks presented are already all too apparent.

Let me conclude by a remark about the decision making process itself. I regret that there was not a full, open discussion of this issue prior to privatization. I cannot see any issue of national security that was served by the secrecy and lack of transparency that surrounded so much of the process of privatization. Greater openness would have subjected the decision to more intense public scrutiny, and that scrutiny, I believe, might well have led to a different outcome, one that I still believe would have been far more in accord with our overall national interests.

Mr. WHITFIELD. Thank you, Dr. Stiglitz.

Mr. Miller.

TESTIMONY OF RICHARD D. MILLER

Mr. MILLER. Thank you, Mr. Chairman. I am Richard Miller a policy analyst for the Paper Allied Industrial Chemical and Energy Workers Union, which, as you know, represents 2,000 worker at Portsmouth and Paducah gaseous diffusion plants, and another 250 workers at the Honeywell-operated ConverDyn facility in Metropolis, Illinois. And with me are representatives of the local unions and workers at the Paducah and Portsmouth plants.

USEC, it is important to understand, is more than a private company simply seeking to satisfy shareholders. In order to privatize USEC, Congress mandated that USEC fulfill important public responsibilities. Privatization would never have been approved by Congress had those important public responsibilities been abandoned. So for USEC today to come in and say these are shackles, these are restrictions that were imposed upon us by the Government you have to understand fundamentally this never would have happened if those obligations had been abandoned.

In fact, they were proposed by USEC in their privatization plan. How in fact did we wind up in the predicament where we are today? At least one point is that every red flag that was raised—and there were numerous—whether it was the conflicts of incentives between shareholders and our national security; whether it was whether you could mesh imports from Russia and maintain and operate two gaseous diffusion plants; whether it was possible to have a viable and economic domestic supply while the company was relying on cash-flow from glutting the uranium and conversion markets; whether it was even anyone did any due diligence to find

out if AVLIS will work. As we know, the joke was you will see Elvis before you see AVLIS. And I wish I had my Elvis mask today.

Today, USEC is in deep financial trouble. Not only was $325 million required to bail out the Russian agreement just after privatization, largely as a result of the impact on the national uranium markets, USEC came back looking for another $200 million precisely as one of the panelists here predicted. USEC is digging itself a deeper hole. It has borrowed another $200 million to finance stock buy-backs, it is paying out dividends in excess of its earnings, and, in fact, it appears as though that stock buy-back was precisely designed to drive down the credit rating in order to escape the Treasury agreement so they could close one, if not both, of the gaseous diffusion plants when the cost lines cross the revenue lines some time at end of 2003.

The junk bond rating has clearly impaired their ability to finance new technology. And selling general and administrative costs have jumped 36 percent in the first 6 month of the current fiscal year, reflecting higher senior management salaries and the addition of blue-chip lobbyists who are plying the halls of government looking for assistance and seeking relief, particularly from this congressional oversight hearing.

The central reason USEC was privatized through an IPO was based on Mr. Timbers' claim that the private corporation was going to promptly deploy AVLIS. Transcripts, however, of the board of directors meetings reveal that the other two companies bidding for USEC didn't think AVLIS was going to work and several board members were troubled that highly sophisticated firms were saying that their basic business plan wasn't going to work.

Well, the independent advisor, J.P. Morgan, upon whom both the USEC board and the Department of Treasury relied for independent advice, said this about those who doubted AVLIS, quote, Let's don't forget what you all heard yesterday was not an unbiased technical expertise advice. Every one of those guys are clearly professional board spookers and they clearly had an agenda which was to convince this board, meaning the Federal USEC board, that what they were saying was right and what you all have done for the past 4 years is wrong. But rather than seek an independent review, the Chairman of the board called on Mr. Timbers, one who clearly had a self interest in the IPO outcome, to disparage his competitor's view of AVLIS. He said every day privatization is delayed is a day we delay the deployment of AVLIS. And yet less than a year after privatization, AVLIS is gone. Now USEC is disclosing its considering closing one of the GDPs in contravention of the privatization act. And I would add none of the significant events that were testified to by Mr. Gensler can be found anywhere in the privatization act or the EPAct of 1992. They got invented out of thin air.

Wall Street is urging closure of a plant on the grounds they would save $65 million a year. And yet experts, some of whom I know have briefed this committee, including John Longanecker, are of the view that USEC will likely have no uranium enrichment industry in this country sometime after 2003 or 2004. So it won't be a debate about which goes first, Portsmouth or Paducah. It will be both.

In July 2001, the restrictions on stock ownership which restricts shareholders from holding more than 10 percent of USEC's stock expire. And at that point if USEC is worth more dead than alive as some suspect as they today, a liquidator will come in and will break them up. Now the question is, what would Congress do in that case? Would they be able to act at that point? Would the administration be able to act? Is there any reason to believe on the other hand that another solution which has been touted, which is a takeover by a bigger more financially solvent firm, might help? They may be more financially solvent, but they have the same shareholder incentives; and for that reason there will be no likelihood that both plants will be operated, there is no assurance the Russian agreement will be implemented if it is not in their economic interest, and the $1 billion to deploy centrifuges will never be coughed up, particularly if it is cheaper to liquidate than it is to invest.

In fact, it is more likely than not that both gaseous diffusion plants will be closed before any new enrichment technology is ever deployed in this country.

I see my time is running down. I would like to point to one other commitment Mr. Timbers made. Many of us doubted both gaseous diffusion plants would last to 2005; and the reason we doubted it was because of 5.5 million SWU a year coming into the country and how was he going to manage both GDPs at the same time. There were options proposed. Mr. Whitfield and Mr. Strickland here proposed legislation to create what we called at SWU bank a way for the Government to play a role taking some of the Russian SWU off the market and metering it in a responsible fashion, but that was rejected.

Yet Mr. Timbers said in letters to us all operating plants considered by USEC require the running of both GDPs until the year 2004. He said I clearly stated no matter what scenario we looked at we will have to keep both plants up and producing for the foreseeable future until at least 2004 just to meet customer demands. And I would like to further clarify these matters in the hope that there would be no further miscommunications by the union about them.

Mr. Rainer reiterated those commitments just 2 months before privatization, and yet here we find ourselves confronting USEC manipulating its balance sheet in order to get out of Treasury agreement by buying back stock and driving down its credit rating. That was a Treasury agreement shot through with loopholes. Everybody knew it. We tried to call the Treasury on it. They would not meet with us. They refused meetings. We tried to meet with the USEC board and you know what USEC's advisors said? The union is complaining about nothing. They continue to complain about nothing.

Mr. WHITFIELD. Mr. Miller, excuse me, if you could conclude.

Mr. MILLER. I apologize, Mr. Whitfield.

Mr. WHITFIELD. Your testimony is very good.

Mr. MILLER. I am sure you will have an opportunity to already have read it. Let me just go to where we are. We have got two choices. We can follow the administration's asleep-at-the-switch approach, which is where we are. And you heard it in the testimony

before us. We can issue severance checks and seek appropriations for cleanup work that might hire 150 people. But there is no administration policy with respect to the problems wrought by this privatization. USEC's signalling it's triggered a significant event. They have told me privately they have triggered a significant event. It is pretty hard to imagine that anybody could believe they haven't.

Moreover, I expect fully that the administration, as Mr. Gensler testified, will continue to sit there like a deer staring in the headlights, while they close the plants. We have heard nothing that causes us to believe they will investigate the breach of contract into which USEC has manipulated itself.

Finally, how do we get out of it? And I'm sure this panel will explore it. We're not abashed to say that you are not going to save the domestic uranium mining and conversion industry unless this goes back in the Government, and the only question is how do we get there.

[The prepared statement of Richard D. Miller follows:]

PREPARED STATEMENT OF RICHARD D. MILLER, POLICY ANALYST, PAPER, ALLIED-INDUSTRIAL, CHEMICAL & ENERGY WORKERS UNION

I am Richard Miller, a policy analyst for the Paper, Allied-Industrial, Chemical & Energy Workers Union ("PACE"). PACE represents 2,000 hourly workers at the Paducah, Kentucky and Portsmouth, Ohio gaseous diffusion plants, and 250 workers at the Honeywell uranium hexaflouride conversion plant in Metropolis, Illinois—the only enrichment and conversion plants in the United States.

SUMMARY

Congress authorized the Administration to privatize the government-owned USEC only on the condition that privatization: (1) would not be inimical to national security; (2) would provide for the continued operation of the Kentucky and Ohio uranium enrichment plants; (3) would provide for a reliable and economic domestic uranium mining, enrichment and conversion industry; (4) would provide for the long term viability of the enterprise; and that (5) the buyer would not be foreign owned or controlled. Subject to the fulfillment of Congressional mandates, Treasury was required to maximize the proceeds from privatization. On July 22, 1998, USEC's Board led, by its Chairman, William Rainer, voted 3-1 (with the fifth member abstaining) to approve privatization via an Initial Public Offering ("IPO").

USEC, Inc. (hereafter, the private company will be referred to "USEC, Inc.") operates the Department of Energy's ("DOE") two uranium enrichments plants in Ohio and Kentucky, the only domestic sources of enrichment capacity in the US. These plants supply fuel generating plants that provide approximately 20% of the country's electricity.

USEC was also vested with the responsibility for the uneconomic, but essential, non-proliferation agreement on behalf of the US government: the U.S.-Russia Highly Enriched Uranium ("HEU") Agreement. USEC markets $475 million/year of blended-down highly enriched uranium derived from Russian warheads to nuclear utilities for use as reactor fuel.

Today, USEC is in financial trouble. It has sought $200 million in government aid to cure the defects that were evident from the outset of privatization. Prior to privatization, the contradictions inherent in USEC's fulfillment of its domestic, national security and shareholder obligations were brought to the attention of USEC's Board, the Treasury Department, the Energy Department and the White House. These decisionmakers knew that implementation of the Russian agreement would displace 47% of USEC's production and drive up production costs at the enrichment plants. These decisionmakers also knew USEC would become the high-cost producer in an oversupplied world market with declining prices, making it difficult to survive against its three other competitors—all government-controlled enterprises. But the entire process was conducted in needless and unlawful secrecy. Smart people are more likely to do stupid things when they close themselves off from outside criticism and advice.

The central reason USEC was privatized through an IPO was based Mr. Timbers' claim that the private corporation would promptly deploy an AVLIS, a new technology that had the potential to make USEC the low-cost supplier worldwide. Transcripts of USEC's secret Board Meetings reveal that the other two companies who were bidding for USEC were dubious, at best, about commercializing AVLIS. One Board member recalled industry joke: "You'll see Elvis before you see AVLIS." Rather than obtain an independent review of the commercial viability of AVLIS, the Chairman called upon an admittedly "very biased" CEO Nick Timbers, to disparage his competitors' views of AVLIS. Less than a year after privatization, the same managers pulled the plug on AVLIS.

USEC has disclosed that it is considering the closure of one gaseous diffusion plant ("GDP"), in contravention of the Privatization Act and USEC's pre-privatization commitments to run both plants through 2004. Wall Street is urging closure, on the premise that USEC would save net $65 million/year [1]. Meanwhile, USEC continues to spend heavily on dividends, stock buybacks, and high executive salaries.

Today our testimony will ask why was privatization was botched so badly, what is the prognosis, and what steps should Congress take next? One feasible solution: establish a government-owned corporation similar to the one establishing USEC in EPAct of 1992, and have this enterprise develop a plan to take over the US Russia HEU Agreement, the operations of the GDPs, and the competent management of USEC's inventories.

USEC, INC. HAS ALREADY JEOPARDIZED FOUR MANDATED PUBLIC RESPONSIBILITIES THAT IT FREELY ASSUMED AS PREDICATE TO PRIVATIZATION

USEC Inc. was vested by statute and contract with important public responsibilities. USEC now portrays these responsibilities as shackles; in fact, they were proposed by USEC in the plan submitted to the Administration on behalf of privatization. Now, only 18 months after privatization, four of these responsibilities have been or will soon be jeopardized, absent government intervention.

- implement a 20 year government-to-government agreement between the United States and Russia to import 5.5 million SWU/year of Low Enriched Uranium derived from nuclear warheads. EPAct of 1992 required that privatization "not be inimical to the common defense and security." (42 USC 2297d-1)
- continue operations of the Energy Department's two gaseous diffusion plants in Portsmouth, Ohio and Paducah, Kentucky (42 USC 2297h-2);
- provide for the protection of the public interest in maintaining a reliable and economical domestic source of uranium mining, enrichment and conversion services (42 USC 2297h-2); and
- provide for the long-term viability of the corporation (i.e. deploy next generation technology) (42 USC 2297h-2).

USEC'S FINANCIAL PLIGHT IMPAIRS ITS FULFILLMENT OF PUBLIC OBLIGATIONS

In the 18 months since privatization, the commitments that were made prior to privatization—especially those to maintain a reliable and economic domestic uranium mining, enrichment and conversion industry—are dissolving amidst the force of USEC's financial difficulties. Objective indicators include:

- USEC, Inc. has announced layoffs/separation of 1450 workers—fully 1/3 of the workforce. Honeywell, the sole domestic UF6 "conversion" plant, has laid off 20% of its workforce since privatization.
- USEC, Inc.'s credit ratings were downgraded 3 notches by Standard & Poors from BBB+ (investment grade) to BB+ (below investment grade or "junk bond" status).
- The Nuclear Regulatory Commission has commenced a review to determine if the credit downgrades will be inimical to the maintenance of a reliable and economic source of domestic enrichment services over a 5-year period.

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[1] BNY Capital Markets, Research Report, April 7, 2000, pp 11USEC will likely shutdown the nation's enrichment industry over the next 3 years. This will result in total dependence on foreign sources for nuclear power plant fuel. 1USEC, Inc's. liquidation, or its gradual transformation into a uranium brokerage operation, both plausible outcomes, would eliminate all domestic production. Some believe that a takeover by a larger company will rescue USEC, Inc. But there is no reason to believe that a takeover will keep two plants open, assure the Russian agreement is implemented, or provide the $1+ billion needed to deploy lower-cost enrichment technology. It is more likely than not that both gaseous diffusion plants will close before a new technology can be designed, licensed and deployed—unless the government is running the enterprise.

- USEC's key to long-term viability—low cost AVLIS enrichment technology—was terminated as uneconomic less than a year after privatization. The non classified portion of the government's $1.7 billion investment was auctioned off at an abandoned K-Mart for less than $1 million.
- USEC, Inc's power costs are up 50% at Paducah since privatization.
- USEC, Inc. projects a steep decline in earnings in the year beginning July 1 ($35-$45 million). This is <10% of the earnings in 1995. The lion's share of 2001 earnings will come from monetizing part of the Energy Department's firm power contracts at Portsmouth.
- Merrill Lynch, one of USEC's IPO underwriters, downgraded its recommendation on USEC, Inc.'s stock to "neutral" and noted that USEC's condition is "worse than we feared."
- USEC, Inc.'s stock price, which measures investors' reaction to its plan for maintaining competitiveness, has dropped to $4.50 from the $14.25 IPO price.

USEC, Inc. is digging an even deeper hole for itself:

- Since privatization, USEC, Inc. borrowed another $200 million, largely to finance the buyback of 30 million shares and pay dividends that exceed earnings. The debt to equity ratio has increased from 33% to 40%.
- Selling, general and administrative costs have jumped 36% in the first 6 months of the current fiscal year[2]. This reflects significantly higher senior management salaries, an increase in headquarters staff, and the addition of blue chip lobbyists who are plying the halls of government looking for "assistance" and relief from Congressional oversight.
- The junk bond credit rating has impaired USEC, Inc's ability to finance new technology. Even with possible technology sharing arrangements with the Energy Department, USEC, Inc. may be bankrupt or liquidated by the time it is ready to break ground on centrifuge technology—assuming it is an economic path forward.
- USEC, Inc. is losing 785,000 lbs of R-114 freon coolant per year. At this rate, USEC, Inc. will run out of its inventories of R-114 by September 2001. R-114 has been banned under the Montreal Protocol, costs about $12/lb and is very scarce. Equipment modifications at Portsmouth are needed for alternative coolants, but these have not commenced. USEC, Inc. will have to close the Portsmouth plant if it does not upgrade for alternative coolant. Without replacement coolant, even the government could not run these plants.

Privatization has jeopardized implementation of the U.S.-Russia HEU Agreement:

- Shipments under the U.S.-Russia HEU agreement were suspended shortly after privatization because of privatization's adverse impact on natural uranium markets. A $325 million bailout was required to restore shipments in April 1999.
- USEC, Inc. informed the Administration and Congress that it would terminate its role as Executive Agent of the HEU Agreement on December 1, 1999, if it did not receive $200 million in assistance. USEC, Inc. argued it deserved assistance to compensate for low market prices. This assistance was denied, in part, because USEC, Inc. advised Wall Street that it was going to announce a stock repurchase plan, and keep paying dividends, and in part because it was unwilling to keep its commitment to operate both GDPs through 2004.

THE ROOT OF USEC'S ECONOMIC PROBLEMS

USEC is a high-cost producer in an oversupplied market competing with government-controlled enterprises. Its production, brokerage, and technology development activities are independently and collectively impaired.

A. Domestic uranium enrichment economics:

Today, USEC is writing new long-term contracts at $80-83/SWU, but its production costs at the GDP's average $95+/SWU. The reason USEC is generating profits at all is that the "order book" of customer contracts assumed by USEC upon privatization included contracts priced at $125/SWU, which has fortunately kept its average selling price at approximately $110/SWU this year. But this cash cow is going to run dry, because the high-priced contracts will expire between 2001 and 2003. At that point USEC will confront negative operating margins on its GDPs, absent a major recovery in SWU prices or dramatically lower electricity costs.

USEC's domestic production economics have been substantially impaired by brokering 5.5 million SWU/year of Russian-origin Low Enriched Uranium ("LEU) derived from nuclear warheads. The HEU deal has displaced 47% of USEC's domestic production. Prior to the Russian Agreement, USEC made 13.6 million SWU/year

[2] SEC Form 10-Q for USEC, pp. 11, February 7, 2000

at the two plants. But USEC has had to cut production by nearly 50%. This raises unit production costs, as there are fewer units of production over which to distribute fixed costs. Thus, even as USEC cut payrolls by 500 in 1998-1999, its average production costs nonetheless jumped from $78.50/SWU in 1995 to $97 SWU in 2000. The additional 850 layoffs slated for July 14, 2000 will cut production costs by approximately $5.50/SWU, but will not restore profitability to domestic production.

Pressured by the need for cash flow to pay out dividends that exceed its earnings, and implementing a 30 million share buyback, USEC has raised cash by selling off its inventory of natural uranium and UF6 conversion products. These aggressive sales have driven down the market price for UF6 conversion services[3]. Without some improvement in the conversion market, major layoffs are inevitable. USEC's sales of government-provided inventory, in short, are eroding the viability of the only domestic conversion plant in the US.

USEC's production costs have also been driven up by summertime spikes in power cost. The Paducah is plant is exceptionally vulnerable to price spikes because it is almost exclusively reliant upon off peak power. However, the impact has been partially offset by sale of blocks of unused firm power at Portsmouth.

B. Brokering the Russian HEU Agreement Economics

USEC pays an average of $88/SWU (including shipping) for the 5.5 million/year of SWU from Russia. These sales are economic when USEC, Inc. fills its order book of contracts valued at as much as $125/SWU. It is not economic when, as now, USEC enters in new contracts at a market price of $80-85/SWU.

USEC is trying to extend the Russian contract at a much lower price, estimated to be 15% below market price ($68-70/SWU). The Russians are reportedly willing to consider market realities, but the size of the price reduction sought by USEC is unlikely to be accepted by the Russians. Moreover, USEC is unlikely to close a deal anytime soon, as the Russians gain leverage the closer they get to the contract expiration date of December 31, 2001. Political developments in Russia also counsel against swiftly concluding a deal for a 20% price reduction.

USEC's marginal cost of production (outside of four summer months) is about $60/SWU Based on the $88/SWU Russian cost, USEC points out this amounts to an opportunity cost of approximately $100 million per year to USEC shareholders (a cost disclosed in USEC's S-1 prospectus). This disincentive, as noted above, drove USEC to threaten to terminate as the US Government's Executive Agent due to the impact to its shareholders.

C. USEC, Inc. Has No Advanced Technology and Cannot be Competitive with GDPs Alone

Although the Energy Department and USEC invested $1.7 billion, AVLIS was determined by USEC, Inc. not to be commercially feasible. With 50 year old GDPs and no proven advanced technology option, USEC, Inc. has no clear path to future competitiveness. With weakened financials USEC, Inc. would find it difficult, if not prohibitively costly, to raise funds to deploy replacement centrifuge enrichment technology that is used by Urenco, its primary European competitor.

THE DETERMINATION TO PRIVATIZE WAS MADE IN DISREGARD OF REPEATED AND NUMEROUS "RED FLAGS" SHOWING THAT PUBLIC MANDATES COULD NOT BE HONORED

Pursuant to Court order, PACE obtained transcripts of the secret USEC Board of Director's meetings. The transcripts show the decision to privatize was made in disregard of red flags that should have given pause regarding the viability of the privatized corporation and its ability to meet national security and domestic mandates. Rather than investigate these warnings, those responsible for privatization too eagerly deferred to the claims of (a) USEC management, who stood to retain their jobs and attain major pay increases and (b) the "independent" financial advisors, who had $7.5 million in success fees tied to a "Yes" vote to privatize.

A. Prior to Privatization USEC Steadfastly Committed to Continued GDP Operation; It Contrived an Escape from these Commitments Within 18 Months of Privatization

Prior to privatization, USEC management vigorously maintained it could implement the US Russia HEU agreement and continue operations of both uranium en-

[3] "Conversion" is the process of converting yellow cake to UF6. UF6 is the feedstock that goes into the GDPs.

richment plants. On April 24, 1997, USEC's CEO Mr. Timbers wrote to OCAW[4] President Robert Wages:

> "All operating plans considered by USEC require the running of both GDP's (gaseous diffusion plants) until the year 2004."
>
> "I clearly stated no matter what scenario we looked at, we will have to keep both plants open and producing for the foreseeable future, at least until 2004, in order to meet customer demands."

USEC refused to produce numbers to show how USEC could operate both GDP's. Mr. Timbers nonetheless scolded the union for doubting management's credibility:

> I would like to further clarify these matters in hopes that there would be no further miscommunications by OCAW about them.

When, on May 1, 1998 OCAW questioned how the statutory requirement to operate both GDPs would be enforced post-privatization, Board Chairman William Rainer wrote:

> "We would remind you that Nick Timber's letter of April 24, 1997 to you advised OCAW of USEC's policy position that both GDPs would operate at least through 2004. This remains our position as we review the various privatization options."

On June 29, 1998, the Treasury Department and USEC released an agreement on Post Closing Conduct ("Treasury Agreement"). The agreement, incorporated in the sales contract, requires USEC to maintain operations of both gaseous diffusion plants through December 31, 2004. On review of the agreement, OCAW wrote to Assistant Secretary of Treasury Gary Gensler that the Agreement was "booby trapped" with loopholes, including the following "significant events" by which USEC can escape the statutory requirement:[5] 1. events beyond the reasonable control of USEC, such as natural disasters; 2. a decrease in annual worldwide demand to no less than 28 million SWU; 3. a decline in the average price for all SWU under USEC's long-term firm contracts to no less than $80 per SWU (in 1998 dollars); 4. a decline in operating margin below 10% in a consecutive 12 month period; 5. a decline in the interest coverage ratio to below 2.5x in a consecutive 12 month period; or 6. if the long term corporate credit rating of USEC is, or is reasonably expected in the next 12 months to be, downgraded below and investment grade rating.

OCAW also asked the USEC Board for the opportunity to appear before it to explain the problems with these loopholes. The request was denied and the Board transcripts show USEC's legal advisors ridiculed OCAW's concerns. Les Goldman of Skadden, Arps stated: "they [the union] continued to complain without giving reason."[6]

Within 18 months of privatization, USEC has engineered a "two-step" escape from the Treasury Agreement.

Step One: Mr. Timbers advised shareholders of his desire to rationalize "global over capacity."[7] In January, 2000 Congressional staff were advised that "USEC anticipates plant closure at either Portsmouth or Paducah to occur sooner than 2004. The January 25 USEC Board meeting discussed the possibility of plant closure."[8]

Morgan Stanley, the lead underwriter for USEC, Inc.'s Initial Public Offering, publically outlined a plan it had privately urged USEC to take to escape the Treasury Agreement:

> With aggressive stock buybacks, the debt could be downgraded to below investment grade. That would be a formal condition allowing USU [9] to shut down one unneeded production plant, which would save $100 million/year annually, according to management. But the physical capability to do all needed production at one plant may be year or more away. And there will be heavy political pressure fighting any such shutdown.[10]

Step Two: USEC followed the script laid out by Morgan Stanley. On February 3, USEC announced that, despite poor earnings prospects, it was repurchasing 20 million shares of stock. On February 4 Standard and Poors immediately downgraded USEC's credit two notches to "below investment grade". USEC verbally advised PACE that a "significant event" had been triggered under the Treasury Agreement.

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[4] OCAW—the Oil, Chemical & Atomic Workers Union—is the predecessor to PACE. On January 5, 1999 OCAW merged with the United Paper Workers International Union to form PACE.

[5] These exceptions were not found anywhere in the USEC Privatization Act.

[6] Transcript, July 22, 1998, pp. 48

[7] Remarks of William H. Timbers, USEC, Inc. Board of Directors Meeting, November 3, 1999

[8] Letter from Senators George Voinovich and Mike DeWine and Representative Ted Strickland to William H. Timbers, January 26, 2000.

[9] USU is the stock trading symbol for USEC.

[10] Stock analyst report by Kit Konolige, Morgan, Stanley, Dean Witter, Downgrade, Another Miss, Catalysts Still Far off, February 4, 2000, pp. 4.

On January 26, PACE wrote to USEC's Board urging it to hold off on rumored stock buybacks and dividend payments because this would compromise the Treasury Agreement. We urged USEC, Inc.'s Board to evaluate whether the corporation could be viable without substantial government assistance. USEC, Inc.'s Board never acknowledged our letter, leading us to question whether Mr. Timbers ever shared it with his Board.

At the same time, Senators Voinovich, DeWine and Representative Strickland wrote USEC's Board:

> "We are forced to question whether USEC entered into the Agreement on Post Closing Conduct in good faith. It appears to us because of USEC's current consideration of plant closure, whether it is Portsmouth or Paducah, that USEC entered into the agreement with fully considering the effects that market supply [from Russia] would have on our country's enrichment activities."

Minutes of USEC's Board meetings from 1996, that had been unlawfully withheld for a year under the Government in the Sunshine Act, reveal that as a government-owned corporation USEC had, in fact, considered plans that included closing a plant prior to privatization. The August 7, 1996 minutes state:

> "the supply mix assumed in the 'Strategic Plan' was not a vote to shut down the plants, but represents a possibility."

This raises concerns about the veracity of USEC's management's representations. The USEC Privatization Act of 1996 (PL 104-134) had already been signed into law on April 26, 1996, with a requirement to continue operations of both gaseous diffusion plants as a pre-requisite for privatization.

On February 22, 2000, PACE verbally advised Treasury officials that USEC, Inc. had triggered a "significant event" under the Treasury Agreement, and that USEC, Inc. had taken steps which appeared to involve bad faith conduct. Treasury refuses to investigate whether USEC, Inc. has subverted the Treasury Agreement in bad faith. Treasury refuses to even acknowledge that a "significant event" has occurred, even as USEC, Inc. announced that fact in February 7, 2000 Securities and Exchange Commission filing. We are at a loss to explain the calculated indifference by the Administration.

The lessons are clear. USEC made promises before privatization, but they were memorialized in loophole-ridden agreements. Protestations that the loopholes were big enough to drive a truck through were summarily dismissed. With the Administration looking the other way, these promises are now being broken.

B. USEC and the Administration Ignored a Congressionally Proposed Solution to the Conflict Between the Russian Agreement and Continued Operations of the GDPs

The twin goals of Implementing the US-Russia HEU Agreement and continuing operations of the both gaseous diffusion plants were never meshed prior to privatization.

Seeking to pre-empt the conflict that has predictably emerged, Representatives Ted Strickland and Ed Whitfield filed HR 3491, the Assisting Acquisition of Russian Material Act, on May 21, 1998, two months prior to privatization. The "Findings and Purposes" spelled out the problem and a possible solution to the problem USEC, Inc. claims unfairly shackles it two years later:

> "The execution of the Russian HEU Agreement will significantly increase the supply of LEU (Low enriched) fuel available in the United States marketplace; and, as a result and in order to balance supply with demand, the privatized United States Enrichment Corporation may have to take actions contrary to or inconsistent with maintaining long-term viability, continued operation of the gaseous diffusion plants, and a reliable and economical domestic source of uranium mining, enrichment, and conversion services, and other statutory requirements . . ."
>
> "The principal responsibility for ensuring the faithful implementation of the United States obligations under the Russian HEU Agreement, which is a government-to-government agreement, lies with the Department of Energy; and the execution of those obligations is an inherently governmental function under the foreign policy of the United States."
>
> "Therefore, the Department of Energy shall, subject to appropriations, acquire directly or from the United States Executive Agent such amounts of the Russian HEU converted to LEU under the Russian HEU Agreement, and withhold such amounts from resale into the private market for such period of time, as may be necessary to fully achieve the national security goals of the United States under the Russian HEU Agreement and to allow a privatized United States Enrichment Corporation to meet the statutory requirements of the privatization."

At the time the bill was filed, USEC management, not wanting to concede the incompatibility of the privatization with operating two GDPs and keeping the Russian

HEU deal alive, rejected the concept offered by HR 3491. They said Congress would never appropriate funds because the Russian Agreement had to be cost free for the government. Ironically, USEC was back 18 months later looking for a way to have the government carry the costs of the Russian HEU Agreement on behalf of their shareholders.

C. The Secret Transcripts Confirm that the Decisionmakers Failed to Perform Due Diligence on the National Security Impacts of Privatization

1. At the time they decided to privatize, the USEC Board and the Treasury Department were on the broadest notice that due diligence required renewed review of the conflict between national security and shareholder interests.

In the weeks before the July 28, 1998 the Administration was put on the most visible notice of the uniform concern of independent experts that privatization would imperil national security. In a *Wall Street Journal* op-ed, Joseph Stiglitz, former Chairman of the Council of Economic Advisors, wrote [11]:

> "That privatization is generally desirable is a core belief of modern economists. Still many economists, including me, oppose the auction [of USEC] which would be the most significant privatization effort in a decade."
>
> "As an economist I believe in the power of incentives. That's why the auction [of USEC] is so worrisome. The management of a privatized USEC would have a responsibility to its shareholders to maximize market value. That goal is likely to conflict with national security. This potential conflict of interest could be a major threat to national security because of the crucial role of USEC in our nuclear non proliferation efforts."

At the time of the Board's final deliberations, nationally recognized experts on the Russian agreement expressed strong concern about the effect of privatization.[12] On June 26, 1998 Senator Pete Domenici—a prominent proponent of privatization—wrote to National Security Advisor Sandy Berger: "In recent days I have become concerned that aspects of the pending sale . . . may have a serious impact on implementation of the HEU Agreement and therefore national security." He added, "I am not certain that a privatized executive agent can still function in the ways necessary to carry out the national security objectives of the HEU Agreement."

Days before the IPO was announced, Senator Domenici learned that USEC would enter the private market with 30 million more pounds of government uranium than was assumed when the 1996 USEC Privatization Act was adopted. Mr. Domenici was concerned that the unanticipated sale of this inventory into the market would lead to a reduction in uranium market price, thereby causing an unplanned reduction in the value received by the Russian government as part of the U.S.-Russia HEU Agreement. These developments "could significantly reduce the Russian Federation's incentive to continue the Agreement."

In fact, the Russian government stated its concern that privatizing USEC with a 70 million pound inventory of natural uranium would significantly devalue a major component of the US Russia HEU Agreement. In a July, 1998 letter to Senator Domenici, Russian Minister E.O. Adamov stated "the execution of the Agreement [US-Russia HEU Agreement] is rapidly deteriorating" as a result of privatization. (Letter attached).

On July 16, PACE asked to address USEC's final board meeting to discuss whether a bailout of the Russian Agreement might be required. This request was denied. Meanwhile 47 members of the House wrote the Administration asking them to stop the privatization.

On July 20, Senator Domenici advised the Vice President's National Security Advisor Leon Feurth, and others that the Administration would be wise not to proceed with privatization, as conceived, because it "could imperil the HEU Agreement". Senator Domenici wrote: "If this means that you would have to resticker the S-1 [Prospectus], so be it."

A July 20, New York Times editorial ("Nuclear Security for Sale) , predicted that privatization "promises rich underwriting fees for Wall Street. But this deal offers little economic gain for the taxpayer and risks big losses for American nuclear security."

2. The Secret Transcripts Show that USEC Board Chairman William Rainer, and USEC's consultants, thwarted due diligence on national security.

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[11] Oped entitled, "This Privatization Proposal is Radioactive," *Wall Street Journal,* Joseph E. Stiglitz, June 2, 1998.

[12] The experts included Tom Neff, the MIT physicist who has been credited with conceiving the HEU agreement; Richard Falkenrath, a national security scholar at Harvard; General Burns, the now-retired officer who negotiated the HEU Agreement with Russia; and as mentioned above, Joseph Stiglitz.

On July 22, 1998 the USEC Board met to finalize its privatization decision. The transcripts show that USEC Board Member William Burton's multiple requests that the USEC Board be briefed by Senator Domenici and National Security staff were denied because "I was told that might inflame the market and so they wouldn't be invited."[13] Indeed, Mr. Burton noted that Board had not even been provided with the Senator's June 20th letter.

In lieu of a briefing by official national security experts, Chairman Rainer asked USEC's private lawyer from Skadden, Arps to brief the Board on national security.[14] Following the lawyer's statements, Board Member Burton reiterated that the Board was being kept in the dark:

> I don't think we have enough information in light of this issue that has risen up. There has been a ton of press, a ton of meetings, everybody who's been involved in it except this Board, and we can't even get a briefing on them.[15]

Shortly following the July 28, 1998 privatization, Russia suspended shipments under the HEU Agreement due to the adverse impacts of USEC privatization on natural uranium markets. At the Administration's request, Congress was asked to appropriate $325 million to bail out the Agreement as part of a deal to offset the harm to Russia from USEC privatization. Cynically, senior Administration officials were planning to seek Congressional bailouts even before the Initial Public Offering was concluded. But this information was conveniently kept away from those who were asking questions on the USEC Board.

3. The Public Concerns Soon Proved Correct—In fact, in October and November 1999, USEC, Inc. threatened to terminate its role as the Executive Agent under the US Russia HEU Agreement if it didn't obtain substantial (up to $200 million) in government assistance. Predictions made by Dr. Stiglitz were confirmed.

This threat induced the US government to seek out replacement executive agents. The Administration quickly discovered that a replacement executive agent would require a subsidy to take on this uneconomic brokerage agreement, and that the conflicts built-in to the privatization, which the Administration it had dismissed were, in fact, quite real. In response to USEC's concerns, (a) the Administration was prepared to offer no more than it would have to expend to hire a replacement executive agent, and, (b) to the credit of the Energy Secretary, only if USEC, Inc. lived up to its previous commitments to keep both gaseous diffusion plants open through 2004. USEC refused to cement the commitment that it had made only 16 months earlier, and further declared it was laying of 850 more workers regardless of government assistance.

D. The Secret Transcripts Reveal that While Serious Doubts Surfaced About Whether AVLIS Could be Commercialized and USEC Could Ever Be Viable, Due Diligence Was Not Performed

The transcripts show that the primary private bidders—Lockheed/Carlyle and General Atomics/Texas Pacific—told the USEC board that they planned to limit investment in or defer deployment of AVLIS. Board members quickly realized that the doubt cast on AVLIS by technically sophisticated bidders called USEC management's claims into question. USEC Board Member Christopher Coburn stated:

> It seems to me that we have a problem, because we have a critical technology which we have based our assumptions on for future performance throughout. We have one source of information. Now finally, we have several independent, if you count these bidders as being independent, sources seem to disagree with us.[16]

Similarly, Board Member Margaret Greene stated:

> we got pretty consistent input from our first opportunity to have external sources give us input, that the AVLIS projections were not realistic.[17]

However, the transcripts show that USEC Board Chairman William Rainer was determined not to secure the requisite independent review of USEC's management claims:

> "[i]t is not practical at this moment to bring in an independent knowledgeable, up to date expert on some of the issues that we heard yesterday that were in conflict with the business plan that management has put together and that this Board has supported now for over four years."[18]

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[13] USEC Board Transcripts, July 22, 1998, pp. 53
[14] USEC Board Transcripts, July 22, 1998, pp. 50
[15] USEC Board Transcripts, July 22, 1998, pp.93
[16] USEC Board Transcripts, June 2, 1998, pp. 177
[17] USEC Board Transcripts, June 3, 1998, pp. 206
[18] USEC Board Transcripts, June 3, 1998, pp. 198

Indeed, Chairman Rainer permitted J.P. Morgan—USEC's ostensibly independent financial advisor—to deprecate the technical analysis provided by management's competition. With regard to the Lockheed/Carlyle presentation of their $1.8 billion bid, J.P. Morgan's Jim Derryberry advised the Board of Directors:

> Let's don't forget what you all heard yesterday was not an unbiased technical expertise advice. Every one of those guys are clearly professional board-spookers and they clearly had an agenda, which was to convince this Board that what they were saying was right and what you all have done for the past four years is wrong.[19] (Emphasis added)

The Lockheed advice, Mr. Derryberry declared, "was very biased."

In lieu of independent review, Chairman Rainer invited USEC management to critique its competition behind closed doors:

> And at the risk of knowing that some of us may be tempted to dilute management's argument about the IPO from the standpoint of potential conflict of interest, we know these people pretty well and each has a factor to divide it by. I nonetheless would like to hear management's view, A, of some of the things that were raised yesterday that opposed to its and our current business plans; because, if management cares to talk about the advantages of an IPO as opposed to an M&A.[20]

USEC's CEO Nick Timbers proceeded to attack his competition:

> We made the decision not to do, specifically not to do what [Lockheed] Carlyle's proposing. And we think that all the test results that we've had over the last 18 months, that it has proven probably to be the right decision.[21]

Mr. Timbers further proclaimed:

- "[AVLIS] is going to be the method by which this company stays viable" [22]
- "every day that privatization is delayed is delay of deployment of AVLIS." [23]
- "we feel confident . . . in the successes of the AVLIS development." [24]

Mr. Timbers assailed his competition in secret while proclaiming he was "very biased":

> I'm very biased. I'm biased to our plan. I'm biased to the AVLIS plan that we have and I'm biased to what I think is a good operating plan that we have.[25]

Mr. Timbers declared that AVLIS was uniformly supported by external studies: [26]

> First of all, there have been extensive external analysis of AVLIS . . . Since 1994 . . . there has been one, two, three, four, five, six, external independent analyses . . . so that there is substantial documentation about whether this is the correct approach, to check our theory.

PACE asked for the analyses referred to by Mr Timbers. When the documents were provided a year after privatization, pursuant to PACE's Freedom of Information of Act litigation, one of the reports stated that:

> Negative cash flows resulting from the deployment of either an AVLIS plant or a centrifuge plant are substantial. In none of the AVLIS cases does the cumulative cash flow turn positive in less than 12 years; the usual turning point is 16-18 years.[27]

USEC in-house and outside counsel—who both had a self-interest in the choice of the IPO [28]—advised the USEC Board that the statutory criteria of "viability" would not be met absent commitment to AVLIS.[29] When challenged, Counsel necessarily acknowledged that continuation of AVLIS did not itself appear as an express statutory requirement. [30] Similarly, USEC Board Members, Treasury and OMB officials (the latter attended all meetings) relied, it appears, on an "independent financial advisor," J.P. Morgan. The transcripts show J.P. Morgan heavily

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[19] USEC Board Transcripts, June 3, 1998, pp. 206-207
[20] USEC Board Transcripts, June 2, 1998, pp. 177
[21] USEC Board Transcripts, June 3, 1998, pp. 215
[22] USEC Board Transcripts, June 3, 1998, pp.242
[23] USEC Board Transcripts, June 3, 1998, pp.244
[24] USEC Board Transcripts, June 3, 1998, pp. 299
[25] USEC Board Transcripts, June 3, 1998, pp. 268
[26] USEC Board Transcripts, June 3, 1998, pp. 211-212
[27] "Advanced Technology Business Assessment," United States Enrichment Corporation, Draft February 21, 1994, pp.102.
[28] USEC in-house Counsel Robert Moore is now Counsel to USEC, Inc. PACE understands that Skadden, Arps, which received over $15 million for its services during privatization, remains as an outside law firm to USEC, Inc. Coincident with Skadden, Arps' statement of its view that AVLIS was essentially a statutory condition, Board Member Burton pointed out that Skadden, Arps was likely not to be retained by Lockheed if Lockheed were chosen (USEC Board Transcripts, June 3, 1998, pp. 224-229).
[29] USEC Board Transcripts, June 3, 1998, pp. 223-224
[30] USEC Board Transcripts, June 3, 1998, pp. 200-202 and pp. 204-206

favored privatization through an IPO. Indeed, it was to be given an additional $7.5 million "success fee" if privatization went forward, above and beyond their basic fee of $80,000 per month.

The secret transcripts show that in the end, with the support of the private consultants, Mr. Timbers' advocacy was central to the Board's choice of the IPO

Only three of five Board members (Rainer, Greene, and Youngblood) voted to privatize through the IPO. At least one of the three (Board Member Youngblood) made plain that his decision was based on the premise—erroneous as it turned out to be—that management's proposal was distinguished by its commitment to AVLIS:

> I will simply make the statement that I think both of them [Lockheed and management] feel that they satisfy these [statutory] criteria. They just do it in radically different ways, one [USEC management] with an investment in AVLIS and the other an investment, a greater investment in the GDPs (existing gaseous diffusion plants).
>
> It is my opinion that I would rather see the investment—having been here since the beginning of this company—to have the proceeds of these billion-plus dollars go toward the reinvestment in AVLIS and the success of the company as [as claimed by USEC management] compared to paying down the debt [as ostensibly proposed by Lockheed].[31]

Despite the substantial uncertainty with respect the feasibility of commercializing AVLIS, and thus doubts about the viability of the corporation, USEC's public prospectus failed to disclose the red flags regarding AVLIS:

USEC's public prospectus ("S-1") filed with the U.S. Securities and Exchange Commission stated that the new corporation would:

> Commercialize AVLIS Technology: USEC plans to complete the development and commence commercialization of the next generation of uranium enrichment technology, AVLIS, which uses lasers to enrich uranium, and which should permit USEC to remain one of the lowest cost suppliers of uranium enrichment services and enhance its competitive position. Commercial deployment of AVLIS is anticipated in 2005.[32]

The public prospectus failed to disclose to the investing public, for example, that: (i) all knowledgeable private bidders had cast doubt on the viability of AVLIS; (ii) independent expertise was not empaneled to review management's self-interested claims; and (iii) the Board relied on the admittedly biased management group to critique its competition.

In sum, the secret transcripts provide compelling testimony that USEC management, with the support of USEC private advisers, made commitments it knew would not be fulfilled. If it conceded that critical statutory requirements could not be fulfilled, privatization—and their large pay and benefit increases—would have been jeopardized.

THE TRANSCRIPTS PROVIDE STRONG EVIDENCE THAT THE PRIVATIZATION OCCURRED BECAUSE OF SECRECY AND CONFLICT OF INTEREST

A. USEC and Other Officials Took a Broad Immunity from Lawsuit and Abused It

The 1996 Privatization act provided broad statutory immunity from suit for any act arising our of privatization:

> "Any stated or implied consent for the United States, or any agent or officer of the United States, to be sued by any person for any legal, equitable, or other relief with respect to any claim arising any action taken by any agent or officer of the United States in connection with the privatization of the Corporation is hereby withdrawn."[33]

USEC managed to take this broad immunity and abuse it. USEC, under the watchful eye of the Treasury Department and OMB, closed the entirety of essentially all USEC meetings in blatant violation of the Government in the Sunshine Act. Then, when OCAW took USEC to court, the Department of Justice, on USEC's behalf, relied on this immunity from litigation to oppose opening the proceedings. It was only in July 1999—following a court ordered deadline—that the Government provided thousands of pages of secret transcripts of the USEC Board meetings. USEC also withheld numerous documents in response to OCAW's December, 1997 Freedom of Information Act request. These documents form the core of this testimony before your Committee.

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[31] USEC Board Transcripts, June 3, 1998, pp. 131-132

[32] Prospectus for 100,000,000 shares of USEC Stock, June 29, 1998, pp. 6

[33] 42 USC 2297h-7(a)(4)

B. The Transcripts Show that the Decision to Privatize through an IPO was Bedrocked on Conflict of Interest

Chairman Rainer's solicitation of the admittedly "very biased" Mr. Timbers to secretly attack his competitors' claims in lieu of the admittedly needed independent review of Mr. Timbers claims, was not merely a conflict of interest, but a conflict that, as Mr. Timbers' subsequent cancellation of AVLIS shows, provides textbook demonstration of the importance of Federal conflict of interest law.

How could this conflict have occurred? Chairman Rainer and Mr. Timbers sought to paper the conflict over with a purported "waiver" of the governing criminal conflict of interest prohibitions.

18 U.S.C. Section 208 ("Section 208")). permits a waiver only where the waiving official finds that the disqualifying "interest is not so substantial as to be deemed likely to effect the integrity of the services which the Government may expect from such officer or employee."

Chairman Rainer's waiver letter for CEO Timbers confirmed that Timbers' financial interest in the privatization decision was substantial (because he stood to significantly benefit depending on the method of privatization, if any, that was chosen). In fact, Timbers, the CEO and President of the new and old company, earned $325,000 when USEC was in public hands. Last February (1999), the board of the newly privatized USEC, Inc. set his base pay at $600,000 per years, gave him a $617,625 bonus and awarded him stock shares currently worth $900,000. [34] In addition, he received a "golden parachute" with 3 years pay and benefits if he is terminated.

As noted above, the transcripts record that Mr. Timbers himself declared that he was "very biased". The letter sought to justify the waiver on grounds that Timbers' services were needed (i.e., expediency), and that Mr. Timbers would be overseen by the Board. There is nothing in the language of Section 208, or to PACE's knowledge, in judicial precedent, that permits a waiver in the presence of an admittedly substantial conflict.

Chairman Rainer's letter declared that Mr. Timbers' admitted bias would be kept in check because the USEC Board would monitor Mr. Timbers' conflict of interest. However, far from keeping conflict in check, the transcripts show—as summarized above—that Chairman Rainer solicited Mr. Timbers' evaluation of USEC management's competition behind closed doors. Mr. Timbers admittedly biased evaluation, in turn, was critical to the Board's split decision to award USEC to Mr. Timbers' IPO team.

PACE requested an investigation by the Public Integrity Section of the Justice Department. In an August 13, 1999 letter to PACE, Mr. Lee Radek, chief of the Public Integrity Section, asserted that since there was a waiver letter, there could be no violation of the conflict of interest law. PACE wrote the Attorney General again asking whether conflicts of interests can simply be papered over with waiver letter, no matter how egregious the conflict.

By letter of September 29, 1999, Mr. John C. Keeney, Deputy Assistant Attorney General for the Criminal Division responded. Mr. Keeney did not take issue with the facts presented by PACE or dispute that Mr. Rainer's waiver was, on its face, in flat out violation of Section 208. Mr. Keeney nonetheless declared:

> Nevertheless, successful prosecution requires that the government prove beyond a reasonable doubt each and every element of an offense. Prosecution of USEC's president would inevitably fail because he sought and obtained a waiver of the conflict of interest.

Thus, according to Mr. Keeney (and Mr. Radek) the Department of Justice's view is that anyone who wants to violate Federal criminal conflict of interest law can do so with absolute impunity by simply papering over the conflict—however raw and even admitted—with a waiver. Conspicuously absent from both the Radek and Keeney letters is any legal analysis, or statutory or court authority in support of their view that the country's bedrock conflict of interest prohibition can be so readily evaded.

In letters of October 8, 1999 and February 5, 2000, PACE, requested the opportunity to meet with Attorney General and staff to discuss determine of the DOJ really intends to modify the 150-year old conflict of interest precedent without any evident basis. Despite repeated inquiries, we have not received a response.

USEC'S PROGNOSIS: WILL ITS PUBLIC RESPONSIBILITIES BE ABANDONED OR FULFILLED?

Fifteen months from now—on July 28, 2001—the statutory restriction on shareholder control of more than 10% of USEC's stock will expire. USEC could be taken

[34] Unjust Enrichment, Nation, December 13, 1999, pp. 4-5

over, and the new buyer will presumably assume responsibility for the HEU Agreement. But there is no reason to believe that a takeover will keep two plants open, assure the Russian agreement is implemented, or provide the $1+ billion needed to deploy lower-cost enrichment technology. It is more likely than not that *both* gaseous diffusion plants will close before a new technology can be designed, licensed and deployed.

If USEC's market value remains, as it is today, far below its breakup value, efficient markets will likely unlock its breakup value through liquidation. Investors could sell off USEC's inventories, receivables, the "order book" of any remaining above market sales contracts, and the HEU Agreement with Russia (assuming it is economic). Over time, the US government would be handed the keys to the Energy Department's uranium enrichment plants. Unfortunately, the US government, at that point, would have watched as investors separated the order book from the plants. Without customers, the plants are not viable.

One prominent analyst stated: "Our bottom line is that making and keeping USEC profitable for the next 5-10 years would require the stringing together of a number of near miracles. In fact, we believe that USEC is unlikely to exist in its present form 2-3 years hence. With 50 year old GDPs and no proven advanced technology option, USEC has no clear path to future competitiveness."

Under the asleep-at-the-switch approach currently followed by the Administration and the bail-me-out approach followed by USEC, the domestic mining, conversion and enrichment industry, as we know it, will disappear this decade.

However, given the non-proliferation imperative inherent in the Russian HEU Agreement, an Executive Agent for HEU deal is required to broker Russian SWU. If USEC's order book is not liquidated, perhaps a brokerage operation will fill these orders with increased Russian imports or subcontract production to fill out the order book.

THE PATH FORWARD: WHAT ARE THE GOVERNMENT'S OPTIONS?

The Administration and Congress have at least three choices with respect to maintaining a reliable and economic domestic supply of mining, conversion and enrichment services, while managing the US Russia HEU Agreement.

A. The Administration's Asleep-at-the-Switch Approach

Aside from issuing severance checks and seeking appropriations for cleanup work that will generate 100-150 jobs, there is no administration policy with respect to the problems wrought by USEC privatization. USEC is signaling that it triggered a significant event under the Treasury Agreement and will announce plant closure as soon as feasible. The Administration is signaling that it has no obligations under the USEC Privatization Act. A cash-hungry USEC that is paying out more in dividends than it is earning will maintain cash flow by liquidating its inventories of uranium and SWU, to the detriment of the conversion and mining industries and USEC's own SWU market. If USEC negotiates a long term reduction in Russian SWU prices to below market, it will be far more economic to broker than operate the GDPs. If USEC goes bankrupt, the creditors will take control of the USEC's order book. The government will confront the nasty question of whether it has to negotiate with creditors in front of a bankruptcy judge over who should control the Russian HEU agreement.

B. USEC's Current Approach to Government Assistance

USEC appears interested in Administration support for extending the Russian HEU Agreement for 15 years at market-based pricing plus a brokerage premium. USEC's financials indicate that, absent dramatic reductions in electricity costs and/or increases in SWU pricing, it will go negative on operating cash flow from the GDPs and likely close both by the end of 2003. USEC appears interested in the government providing financial assistance to deploy new technology, through in-kind DOE research, buildings and equipment, and loan guarantees.

Long term investments in new technology—if feasible—require that USEC is not liquidated, nor bankrupt, before completing the construction project in the 2006-2007 time period. Under the current pathway it is likely that both GDPs will be closed before any new technology is deployed and operating successfully.

C. It is Time to Create a Government-Owned Corporation to Assure the Public Interest is Not Further Compromised

The Administration and Congress should develop a plan to create a new government-owned corporation modeled after the original United States Enrichment Corporation which was established under the Energy Policy Act of 1992.

Initially, this new corporation would be charged with assuming the role as an Executive Agent for the U.S.-Russia HEU Agreement to guarantee performance of the Russia HEU deal. USEC could purchase SWU from the Executive Agent up to the 5.5 million SWU that it needs to fill orders. The Corporation would be authorized to request appropriations, as necessary, to assure the full implementation of the U.S.-Russia HEU Agreement. However, the Executive Agent could stockpile SWU if deemed necessary, to maintain security of supply, and sell it consistent with the 1996 USEC Privatization Act.

The government-controlled corporation, in cooperation with the Secretary of Treasury and Energy, would evaluate and develop options for maintaining domestic production enrichment capacity, if and when, USEC fails to do so. The government-owned corporation could operate the gaseous diffusion plants, develop, test and deploy advanced technology, and utilize the DOE's electricity contracts.

Mr. WHITFIELD. Thank you very much.

Mr. Stiglitz, I had referred earlier to a letter that you wrote to the President and the Vice President—I'm sorry, Dr. Neff wrote the letter expressing similar concerns to what you had. But in your testimony you talk about the fact that there was a lack of transparency and lack of open discussion. Did you have discussions with Treasury officials about this prior to the decision being made to privatize?

Mr. STIGLITZ. Oh, within the administration, there were a large number of discussions. And all the issues that I raised and more we tried to bring forward.

The general stance was this is a done deal, why are you fighting something that's already a fait accompli. And we were just a little bit more obstinate because we thought what was at issue was extremely important. But what I was referring to in lack of transparency there was very little public discussion. We found it very difficult. And the ethics was that within the White House you don't discuss public issues unless there is a decision to make in public. And so the view was that we could discuss it within ourselves, but if there is any disagreements, or these issues, nobody else should be brought into the decisionmaking process.

Mr. WHITFIELD. Were there other members of the National Security Council that had the same reservations that you did?

Mr. STIGLITZ. There were other people within the national security community, but not within the National Security Council. I might add that after I left the administration, we had a meeting at the Council of Foreign Relations in New York of a large number of national security experts on the issue of nonproliferation, and there was not a single one that could identify a positive argument for privatization.

Mr. WHITFIELD. Right. Mr. Graham, in your testimony you talked about how your industry is slowly being driven out of business. Someone, I can't remember who, talked about how USEC is using both its control of uranium and the only enrichment facility in the country to obtain business and that they're using that excessive power to drive other people out. Would you elaborate on that a little bit.

Mr. GRAHAM. Mr. Chairman, I would think that the answer to that question is that since USEC is the dominant player in the fuel cycle representing over 50 percent of the value chain of nuclear fuel, that they have the ability with their large inventory of uranium and conversion services, to couple these products together to go to customers and sell them the final product, which in this case

is the three components, uranium conversion and SWU, as EUP. And the value of that EUP is such that if you lower it just a little bit, you are able to put a great deal of pressure both on the uranium and conversion components and thus take a larger market share.

Mr. WHITFIELD. And they did receive UF6 from the Government as well. Correct?

Mr. GRAHAM. The bulk of the material that was transferred to them that was in their inventory at the time of privatization was in the form of UF6.

Mr. WHITFIELD. So that eliminates the need for your service?

Mr. GRAHAM. Exactly, sir.

Mr. WHITFIELD. Dr. Brewer, you had discussed how USEC is selling its uranium, and that's one of the things that's really keeping them afloat right now, isn't it?

Mr. BREWER. Yes, that's correct. It's like if you were running a company, as I did for 10 years as CEO, and you had—you were relying on your current profitability from operations that existed in the past their contingency reserves put on the balance sheet and then when those are exhausted or when you are no longer obligated, you drop those into the P&L, it is like that. If you are not profitable on current operations, you are in bad trouble. And this did not happen to me, but I saw it happen to other business units in combustion engineering.

Mr. WHITFIELD. But they are basically cannibalizing themselves.

Mr. BREWER. Yes, they are eating their seed corn, and it is like living on principal rather than earnings.

Mr. WHITFIELD. And they are losing market share; is that correct?

Mr. BREWER. Yes, they are losing market share. They are losing backlog, and most important is the quality of the backlog. In other words the profit margin embedded in the backlog is south of costs. And you can see from the figure that they're negative now. The only thing that's—that's hiding this or concealing it is the sale of the uranium stockpile.

Mr. WHITFIELD. And Mr. Timbers talks a lot about the Russian agreement, how harmful it has been to his company; but his production costs now are even greater than what he is buying it for, isn't it?

Mr. BREWER. That's correct. In the early days of the Russian agreement, there was—the marginal cost of production was less than the price of the Russian uranium in dollars per SWU. The marginal cost was about $50 an SWU and now it is $75.

But, moreover, most important is that you cannot go out and purchase the power to produce that 5.5 million SWUs from the Russians; you cannot replace that purchase because you have to go out and contract for power probably at 3 or 4 cents a kilowatt hour. They are paying about 2.1 cents per kilowatt hour now. I'm paying in Virginia 9 cents a kilowatt hour. So you know——

Mr. WHITFIELD. I think Mr. Moniz and others talked about if their electrical costs go up just a cent, it can make a gigantic difference to them.

Mr. BREWER. Yes, if you go out and try to contract to replace that Russian import, the cost is going to be astronomical. So when you

hear them tout and make this excuse, this "dog ate my homework" excuse, that it's the Russian deal that's the blame, it's false.

Mr. WHITFIELD. Well, it's obvious that they're in a very serious condition right now and all of us have a lot at stake here and we are going to have to try to come up with some answers.

Mr. Stupak.

Mr. STUPAK. I've been sitting here some 5 hours, and we had to prepare for this hearing, and I'm just looking at this whole thing. What gain was there for the Government or the taxpayers in this whole deal? I don't see a silver lining here for anybody. You guys are on the way out trying to keep your head above water. We have extra uranium coming here and just sitting here, and here is this contract that we entered into and there is supposed to be some benefit for the Government, the taxpayers if you will of this country; and I don't see any. Am I wrong? I mean, Wall Street made a few bucks off of it, I guess. That's about it.

Mr. Stout, when I looked at your letter that you received from DOE in February of this year it seems to say that it can't do anything about USEC's dumping of uranium except to talk to them about it. Is that your impression? I don't mean to put words in your mouth. That's the impression I got.

Mr. STOUT. That could well be the case. I guess to this point no specific concrete proposals have been forwarded by DOE.

Mr. STUPAK. Other than talk to them? You know, what do you think—I will ask Mr. Miller on down, what do you think government should do here? What do you think we in Congress should do? Let's have an open discussion here a little bit about this. There is no benefit to us. What do we do? Tear it up and start all over?

Mr. MILLER. Well, you have a tricky problem because the shareholders control; and if they go bankrupt, you will do business with the creditors.

Mr. STUPAK. Well, if we don't give them $200 million bailout, there won't be anything to——

Mr. MILLER. Well, they have uranium inventories they could liquidate to carry on so they at least continue to cover the interest on their debt for some time. But I think one of the things that is important to keep in mind, the Russian agreement—I would beg to differ slightly with Dr. Brewer on the impact on USEC. A report that was done—this was based on public sources by Energy Resources International, shows that when you cut your production by 47 percent, as has happened to USEC in order to accommodate that important Russian agreement, you wind up raising your unit costs. As a result, we have seen labor costs per SWU climb from $15.70 in 1995 up to $27.70. I can assure you it isn't like Mr. Timbers where we got a pay increase. Okay? It is because you are amortizing those costs over fewer SWU, and there is a certain point where you cannot cut workers as much as you cut production and maintain safety.

So as a result, I do think that government has a role here to ensure the security of supply under the Russian agreement and security of supply with respect to maintaining a domestic industry. It is not economic for a private sector firm to do it whose first priority is to take care of their shareholders, and that is why I think some

kind of alternative structure has to be developed that takes this out of the private sector.

If you don't care, if Congress makes the conclusion that it doesn't matter whether we have a domestic industry and if the uranium industry is not viewed as important, if the conversion industry is not viewed as important and you don't want a domestic source of enrichment and you prepared to be dependent upon foreign suppliers, then put a fork in it. If you don't come to that conclusion, then I think government has a role here.

Mr. STUPAK. Anyone else? Dr. Brewer?

Mr. BREWER. I would suggest that, first of all, that you separate the national security and diplomatic roles that USEC has been given, which they sought and were given, from USEC as a standalone business. And let the CEO go run that business, if he can, and bring the other functions back to the U.S. Government, the functions of Russian importation et cetera.

Second thing that should be studied is for the Department of Defense and the Department of Energy to reclaim beneficial control over one of the GDPs in the national interest, as a national security matter. If it's not needed for production of LEU, then—which it probably is not since we do not have the cold war anymore you don't need it for weapons and you need very little for Navy use, you could run it in a hot stand-by condition. But take one GDP and keep it in a hot stand-by condition under the control of either DOE or DOD. I would prefer DOD, but—but at any rate, separate this terrible conflict of interest you have got between the national security and running a business going through the head of one former bond salesman.

Mr. STIGLITZ. Let me just—I think the two points that Dr. Brewer raised are the essential ones that the national security issue is first priority, getting that taken back into the Government. It is a little more complicated though because unless the government wants simply to stockpile it, most—a lot of the contracts in the past have been through USEC, and that's one of the assets which they have. So this would have to be a accompanied, I think, by this kind of detailed security analysis of how important is it to the United States to maintain a production, a conversion, a mining capacity in each of these areas.

And I would suspect they would decide that it is important to keep some level of capacity and the question is what level of capacity. And then ask, having decided that how do we go about—what are the impediments to doing that? And almost surely the answer will entail some restrictions on the sale of this huge stockpile. Any industry, if all of a sudden we took our oil stockpile in a normal circumstance and started selling it all of the sudden, it would have a shock effect on the oil market. It wasn't put there as a method of bailing out a firm; it was put there for a whole set of national strategic reasons to be sold over a longer period of time.

So it is probably the case that you have instruments of control under the privatization; but you may not, in which case you will have to have legislation that would address how do you control the pace of sale of those stockpiles.

Mr. STUPAK. I see my time has expired. My follow-up question was going to be how much is it going to cost us, but I guess that is for another day. Thank you, Mr. Chairman.

Mr. WHITFIELD. Mr. Strickland.

Mr. STRICKLAND. I want to thank this panel. I only wish that Mr. Timbers and Mr. Gensler from Treasury were sitting in this room listening to what you have to say. These are important matters, and I hope to God that they at least read your statements.

You are very credible and believable people. I was especially struck by your comments, Dr. Stiglitz, regarding the secrecy. Before privatization, I told the Vice President that it was impossible for me to know if anything illegal or unethical was happening, but that there was so much secrecy surrounding the process that it was impossible to know for sure. And then he referred me to Mr. Gensler, and others within the administration. And I asked for information, and it was refused me. Even that waiver letter that I made reference to earlier in this hearing I received only after filing a freedom of information request, a document that should have been available to every American citizen. And that's just one example of the secrecy that surrounded this process.

Now you are all credible people. Dr. Stiglitz, you are a person that is well known in the economic world. I want to ask a question. We've talked about what to do. If, in fact, a national security matter and an economic security matter is at risk here, and if privatization at least as it occurred was a bad idea and it was carried out poorly, why not reverse that process? And I would like to ask each of you if you would like to see this government resume responsibility and ownership and control of this industry. I'm not asking you if we can or how we could do it, but I'm first of all asking you if that's something you would like to see.

Mr. GRAHAM. Congressman, from the conversion industry, life before privatization was a level playing field. We could compete with all the competitors on an international basis. In the current form, we cannot compete and cannot survive; and we would vote for it to be returned to the government.

Mr. STOUT. I think it is good energy policy to ensure that we always have a strong domestic uranium enrichment corporation. I guess from what I've learned in the past and what I've heard today, I have serious doubts about whether that's going to be the case much longer under the current situation.

Mr. BREWER. Mr. Strickland, I would take it back to a government-owned corporation. I would take it back that step. I would not take it all the way back to the business I had to run as assistant secretary because you have so much dysfunctionality in the annual appropriations cycle and the section 161(B) and inability to compete.

But, yes, I would take it back to a government-owned corporation, something like a COMSAT.

Mr. STIGLITZ. I agree. I think the inherent conflicts of interest between public and private purposes that are virtually impossible to address through regulatory mechanisms make it very difficult for it to be a conventional private enterprise, particularly given the global market structure in which it is embedded.

Mr. MILLER. Mr. Strickland, I guess I've already identified that our preference would be a government-owned corporation as well. This committee marked up and reported a bill, an EPAct of 1992, that created a government-owned corporation. What the logistics would be perhaps would be for another day, but we would strongly support putting this back in the Government.

Mr. STRICKLAND. Thank you. I think at least from my perspective what we have heard today casts serious doubt upon the credibility of the management of USEC and their intentions. The word "cannibalization" has been used here. We are talking about selling off assets in order just to stay alive perhaps for a short period of time. We have talked about a management that has a golden parachute in place. And so, Mr. Miller, I want to ask you a question that I think gets to what may be a very large problem here. And it has to do with concerns that may exist regarding an adequate supply of coolants for the GDP plants.

How concerned are you about that matter? And the reason I ask is it is because if there is a management that is serious about maintaining these facilities, continuing to operate this industry, then they've got to think ahead in terms of what is required of them. And my understanding is that this is a serious problem; that the freon issue is a serious problem; that they at this very moment should be engaged in planning for how to deal with this problem. And if they are not doing it, then it makes me wonder if they're serious about maintaining the viability of this industry or if they're just going to rape it for all of its assets and then walk away leaving Uncle Sam and the taxpayer holding the bag. Would one of you answer that, please.

Mr. STIGLITZ. I have to run catch a plane, can I be excused?

Mr. WHITFIELD. Yes, sir. Thank you, Dr. Stiglitz, for being here. We are sorry we detained you.

Mr. STRICKLAND. Thank you, Dr. Stiglitz.

Mr. MILLER. Well, Dr. Brewer, our assessment of this at least is that unless we have missed something from USEC management, their inventories of R114 run out. They have about 1.25 million pounds in inventory. It is almost impossible to buy; it has been banned under the Montreal Protocol, properly. The problem is they run out in September 2000 at their current leak rate. Unless the leak rate is dramatically slowed, they should be making mechanical upgrades to permit them to use replacement coolant. We have seen no construction work which would cause us to believe that. And if the keys were turned back over to the government to run these plants, they couldn't run them either because there is no coolant.

Mr. BREWER. One of the reasons why the production costs for GDPs has gone up from $50 an SWU up to $95 is because lack of maintenance and lack of attention to detail and training and so forth. And I won't go all the way and say they're treating it like a cash cow or milking a cash cow, but it's close.

Mr. WHITFIELD. Any further questions, Mr. Strickland?

Mr. STRICKLAND. No, thank you. Thank you, Mr. Whitfield, for your patience.

Mr. WHITFIELD. Well, I want to thank the panel. We looked at the management of USEC, and in one of their board meetings

when they talked about going to an IPO they said their debt would never exceed 25 percent of their market capitalization, and today it's about 110 percent. They said their market share was going to increase; it's decreased. They said the SWU prices were going up; they're going down. They said the production costs were going down; they went up. They said that they were going to save the enrichment business with AVLIS technology, and no sooner were they privatized than they scrapped it.

We are damaging our uranium industry and our conversion industry of uranium. And we have a lot of individuals and their families who are suffering as a result of it. And we have placed this Russian agreement in jeopardy in a way.

So I think we have a very serious problem here, and your testimony has been quite helpful as we explore some options and some ways to try to deal with this. I want to thank you very much for your time. It has taken about all afternoon. I apologize for that. We thank you and we look forward to working with you as we try to address this problem.

Thanks. The hearing is adjourned.

[Whereupon, at 7:01 p.m., the subcommittee was adjourned.]