

of circumstances and to balance Fund security while obtaining the maximum possible return under the circumstances.¹⁶⁹ Accordingly, we will not adopt Alternative No. 3.

Nor will we adopt Alternative No. 1: continuation of Black Lung restrictions. Commenters have persuaded us that public utilities' decommissioning requirements can best be funded by permitting investment of ratepayers funds according to Alternative No. 2, a reasonable person standard with no specified investment restrictions. We agree that it is possible to protect the integrity of an investment portfolio as a whole by investing in various classes of assets with offsetting risks. This strategy will allow investment managers to adjust quickly to financial and market conditions and should, over time, produce higher returns than Black Lung investments and lower the amount of ratepayer funds necessary for decommissioning.

The reasonable person standard, with its emphasis on a balanced portfolio and offsetting risks, is a very sophisticated investment approach, requiring considerable expertise to implement successfully. Public utilities must choose trained, experienced, professional investment managers who are skilled in the art of offsetting risk, and must ensure that they act with the level of skill, care, diligence and caution expected of a professional planner in light of the purposes, terms, distribution requirements, and other circumstances of the Fund.

Several Commenters observe that Black Lung investments have a place in a balanced portfolio under appropriate circumstances.¹⁷⁰ They state that it would be reasonable for a prudent investor to use these more conservative investments to offset the higher risk of other investments. And Commenters recognize that, as the date at which the utility must meet decommissioning expenses comes closer, greater liquidity

and more conservative investments should be the norm of the portfolio balance.¹⁷¹ We agree that Black Lung investments still have a place in a Fund's investment portfolio under the unconstrained, reasonable person investment approach. We also agree that a reasonable approach would be to decrease the percentage of equity investment in a portfolio, and increase the amount of lower risk investments, as the time for expending the funds approaches.

The Alternative that we are adopting in the Final Rule dictates our choice of the precise definition and content of the reasonable person standard. We will define a "reasonable person" as a "prudent investor." We choose the prudent investor standard because it does not focus on any single investment but rather insists on an evaluation of the entire portfolio.¹⁷² This is consistent with the unconstrained reasonable person investment approach. If investment managers are to properly implement the reasonable person investment strategy, without restrictions, they are going to need the flexibility that the prudent investor standard provides.

We see no need to incorporate the ERISA standard into this proceeding. ERISA deals with a fundamentally different liability. Rather, we will adopt Edison Electric's, Cooperatives', and Pennsylvania Commission's recommendation and base the prudent investor standard on the principles set forth in § 227 of the Restatement (Third) of Trusts (1992).¹⁷³ This will accomplish the objective of allowing for flexibility of Fund investment, without importing into Fund investment standards all of

the law surrounding employee pension funds.

Also, it is unclear that the ERISA standard is sufficiently exact to adequately address the contingencies of nuclear plant decommissioning. ERISA requires of a fiduciary "familiarity" not "expertise" and requires diversification of investment assets not to prevent but merely to "minimize" the risk of large losses to the fund. The Restatement (Third) of Trusts is more rigorous in its demands on a fiduciary.¹⁷⁴

The prudent person standard, which we also considered in the NOPR, focuses on each investment individually and proscribes certain investments as too risky.¹⁷⁵ This standard is inconsistent with an investment strategy of offsetting risk, which is at the heart of the reasonable person investment approach.

The prudent person investment standard would not allow fiduciaries to rapidly adjust to ever changing market and financial conditions as they must if they are to correctly manage the Fund portfolio as a whole.

X. Conclusion Regarding Selection of Alternative

For the reasons given immediately above, we are adopting for Fund investments Alternative No. 2, the reasonable person standard, without constraints. We define a "reasonable person" as a prudent investor, as delineated in the Restatement (Third) of Trusts (1992).

XI. Environmental Statement

Commission regulations require that an environmental assessment or an environmental impact statement be prepared for any Commission action that may have a significant adverse effect on the human environment.¹⁷⁶

¹⁷¹ E.g., Duke Comments at 5 ("[I]t would be logical to have higher equity exposure in the early years of the Fund than in the concluding years. . . ."); Entergy Comments at 3 (Equity phase-down should begin five years before expected license termination); New York State Comments at 6; Northeast Utilities Comments at 12 and Exhibit C at 1 (Under normal circumstances equity percentage of Fund portfolio should decrease as decommissioning cash outflow approaches [12]; Phase-out of equity investments to begin five years before the expected need for significant decommissioning expenditures [Exhibit C at 1]); Nuveen Comments at 11 (Percentage of equity investment should decline as date of expenditure of substantial portion of Fund assets approaches); Pennsylvania Commission Comments at 12, Reply Comments at 9 (returns and invested principal should be moved back into relatively secure instruments before decommissioning); Wisconsin Power & Light Comments at 2 (The expected liquidity needs of the Fund should determine the reduction in equity exposure.).

¹⁷² See Restatement (Third) of Trusts § 227 (1992).

¹⁷³ See Edison Electric Comments at 4-5; Cooperatives Comments at 7-12; Pennsylvania Commission Comments at 15 and Reply Comments at 14.

¹⁷⁴ For example, Section 227 of the Restatement (Third) of Trusts includes "passive strategies" as a practical investment alternative that Trustees must consider. The Restatement points out that investing in index funds that track major stock exchanges or widely published lists of publicly traded stocks offers pricing security and economies of purchase in essentially efficient markets. See Restatement (Third) of Trusts, § 227, comment h., Prudent Investment: Theories and Strategies (1992).

¹⁷⁵ See Restatement (Second) of Trusts § 227 & comments a through o (1959). In the NOPR, the Commission also referenced the standard that it uses to determine the prudence of specific costs, citing *New England Power*, *supra*. See 59 FR 28,300, IV FERC Stats. & Regs. Proposed Regulations 32,853-54. In the NOPR, we recognized "that what we are concerned with here is a different factual setting." *Id.* We agree with Edison Electric that "pursuing a prudent investment strategy is not necessarily the same thing as incurring a prudent cost." Edison Electric Comments at 16.

¹⁷⁶ Regulations Implementing the National Environmental Policy Act, Order No. 486, 52 FR 47987 (Dec. 17, 1987), FERC Stats. & Regs.,

¹⁶⁹ Northeast Utilities Comments at 10-11.

¹⁷⁰ E.g., Carolina Power & Light Comments at 8 (Because of long time-horizon and sensitivity to inflation, Funds should invest in common stocks as well as in fixed-income securities); Cooperatives Comments at 9 (A diversified portfolio should have its assets dispersed among a variety of equities and fixed-income investments); Indiana Michigan Comments at 2 (Black Lung or other conservative investments are always acceptable components of the Fund); Northeast Utilities Comments, Exhibit C at 1 (trust to maintain a balanced portfolio consisting of equity and fixed-income securities); Nuveen Comments at 3 (Fund portfolio should contain a targeted range of fixed-income and equity securities to manage market risk).

Edison Electric goes further than this and insists that Black Lung investments are not imprudent and continue to be an accepted investment alternative. Edison Electric Comments at 15.