ORDER NO. 76292

IN THE MATTER OF THE INVESTIGATION INTO AFFILIATED ACTIVITIES, PROMOTIONAL PRACTICES AND CODES OF CONDUCT OF REGULATED GAS AND ELECTRIC COMPANIES.	* * * *	BEFORE THE PUBLIC SERVICE COMMISSION OF MARYLAND CASE NO. 8820

Before: Glenn F. Ivey, Chairman
Claude M. Ligon, Commissioner
Susanne Brogan, Commissioner
Catherine I. Riley, Commissioner
J. Joseph Curran, III, Commissioner

Filed: July 1, 2000

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EXECUTIVE SUMMARY

I. Introduction

This Order, along with others issued during the restructuring proceedings, is designed to promote the creation of competitive electric and gas markets with appropriate customer safeguards. Building upon recent Commission decisions and the passage of recent legislation, this Order directs gas and electric companies to implement rules designed to ensure an appropriate degree of separation from their affiliates.

The Commission takes these actions for the following reasons: (1) to prevent cross-subsidization of affiliates and maintain the financial integrity of regulated utilities; (2) to prevent affiliates from unduly exploiting any competitive advantage due to their relationship to the utility and help foster competitive markets for gas and electricity; (3) to minimize the sharing of confidential information; (4) to protect consumers and ratepayers; and (5) to prohibit discrimination by utilities in provision of utility services. The Commission sought to achieve a reasonable balance between the positions of the parties and the mission of the Commission along with the various statutory directives, which include the provision of just and reasonable rates, and maintenance of safe, reliable distribution systems.

II. Discussion

A. Standards of Conduct

The Commission modifies the standards of conduct for transactions between a utility and both core and non-core affiliates that were adopted in Case No. 8747. Because of recent changes in energy markets and the move towards customer choice, the Commission concludes that new standards are required. Rather than choose the extremes of strict separation between utilities and affiliates on the one hand, or maintain the standards of Case No. 8747 – which have proven to be less effective than originally expected – the Commission chooses a middle course. The Commission retains the core/non-core distinction established in Case No. 8747. For example, previous restrictions on tying arrangements, discriminatory treatment towards competitive suppliers and joint sales leads will remain in place. However, joint promotions, marketing and advertising between a utility and its affiliates are now prohibited.

The Commission, yet again, endorses asymmetric pricing for assets, and permits utilities and their affiliates to share certain employees performing general corporate tasks and services. The Commission finds that these principles can be beneficial to ratepayers, but do not enhance market power.

B. GENCO Code of Conduct

Except for a separate GENCO code of conduct, gas, electric and combination utilities should be subject to the same rules and practices adopted in this case. For electric companies, this Order lets stand the GENCO codes of conduct adopted in the Baltimore Gas and Electric Company ("BGE") and Allegheny Power System ("APS") individual settlements. The BGE GENCO code of conduct will be adopted as the generic code of conduct applicable to any utility operating in Maryland that does business with any company affiliate that acquires electric generation assets in the future.

C. Cost Allocation Manual (CAM) and Reporting Requirements

To address concerns about cross-subsidization, and to ensure that ratepayers receive all benefits to which they are entitled, the Commission will require most energy utilities to file Cost Allocation Manuals no later than November 1, 2000. More extensive reporting will be required to ensure that the CAM methodologies are being followed. In addition, the Commission will closely monitor the sharing of employees, loans and other financial transactions between a utility and its affiliates.

D. Royalties and Disclaimers

If a utility permits its affiliate to use the utility's name and logo, the Commission finds that it is appropriate, in principle, to impute a royalty to the regulated gas and electric utilities: (1) for the value of the name and logo of a utility; and (2) for unquantified benefits conferred upon affiliates because of lack of complete separation. This finding builds on precedents established in several prior Commission cases and represents the Commission's continuing efforts to appropriately allocate the cost of benefits and services between utilities and affiliates to reduce and eliminate cross-subsidization. The Commission will docket separate proceedings to determine: (1) the appropriate royalty to be imputed to utilities for use of the name and logo; and (2) the unquantified assets that have been transferred from a utility to its affiliate(s). Such valuation shall be effective as a revenue adjustment to the cost of service effective July 1, 2000.

In addition, to minimize customer confusion the Commission will require prominently displayed disclaimers when an affiliate uses the utility's name or logo. The disclaimers must state that the utility and the affiliate are separate entities, and that the Commission does not set the affiliate's prices.

E. Waivers and Exemptions

In recognition of the unique circumstances of the various energy utilities in Maryland, the Commission provides for certain waivers and exemptions to the rules adopted in this Order. Municipal utilities and Eastern Shore Gas Company are exempt from these rules. Cooperatives and small utilities are covered by these rules, but may request a waiver of these rules if they are unduly burdensome.

III. Conclusion

This Order establishes reasonable standards of conduct for electric and gas utilities and their affiliates in light of emerging competitive energy markets. Further this Order will serve to foster the development of competitive retail electric and gas markets within the State, maintaining the financial stability of regulated utilities, and promote opportunities for economic benefits for all customer classes.

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I. BACKGROUND

The Public Service Commission of Maryland ("Commission") docketed this case on July 26, 1999 to examine issues relative to the relationship and conduct between Maryland's utilities and their affiliates. The primary concern of this case is to ensure that ratepayers of the regulated entities do not subsidize an unregulated enterprise. In addition, Order No. 75381 directed the parties to address any remaining issues from Case No. 8747[1], which focused upon affiliated activities and standards of conduct and Case No. 8677, which focused upon promotional practices. Finally, the passing of The Electric Customer Choice and Competition Act of 1999 ("the Act") [2] and the Natural Gas Supplier Licensing and Consumer Protection Act of 2000 ("the Gas Act") [3] provided further impetus to the Commission's continuing effort to address changes taking place in the electric and gas industries and how these changes affect utility/affiliate interactions.

In Case No. 8577,[4] an investigation into the relationship between Baltimore Gas and Electric Company ("BGE") and its gas marketing affiliate, BNG, the Commission adopted four cost allocation and transfer pricing principles to be applied by BGE and

[1] *Re Affiliated Transactions and Affiliate Standards of Conduct of Companies Providing Gas or Electric Service in Maryland*, Case No. 8747, Order No. 74038; 89 MD PSC 54 (1998).
[2] Public Utility Companies Article, *Annotated Code of Maryland*, Section 7-501 et seq.
[3] Public Utility Companies Article, *Annotated Code of Maryland*, Section 7-601 et seq.
[4] *Re Baltimore Gas and Electric Company; Small Business Coalition for Fair Utility Practices v. Baltimore Gas and Electric Company*, Case No. 8577, Order No. 72107, 86 MD PSC 225 (1995).

BNG relative to transfers of assets, services and personnel between the companies. These principles were designed to ensure that BGE ratepayers would not pay for the activities of the utility affiliates and provide that:

- cost allocations should be made on the basis of a fully distributed cost allocation methodology;
- the cost of services provided by BGE to its affiliate should be based upon the full cost of such services, including any indirect costs;
- the fair market value of services which reasonably could be marketed by BGE to the public must be allocated as the imputed cost to its affiliate; and
- asymmetric pricing principles were adopted for transfers of assets between the utility and the affiliate.

The Commission concluded that the adoption of these principles "will ensure that utility operations do not subsidize the subsidiary, and they will result in market prices being paid where appropriate."[5] In Case No. 8709, the Commission expanded upon this basic framework and adopted 12 standards of conduct to be followed by BGE in its relationship with BNG.[6] These standards included rules requiring BGE to:

- contemporaneously provide gas system information to competitive gas suppliers that it provides to BNG;
- offer equal prices;
- provide gas sales and delivery on similar terms;
- apply its tariff in a similar manner to both BNG and suppliers;
- and process service requests in a similar manner.

[5] *Id*. at 234. In addition, the Commission affirmed its finding in Case No. 8487 which required BGE to reflect operations of BGE's Gas Appliance and Service Department above-the-line.
[6] *Re BNG, Inc.* Case No. 8709 Order No. 72523, 87 MD PSC 43 (1996).

In addition, the Commission made other findings to reduce cross-subsidization, to protect customer pricing and to help create a competitive natural gas market. Specifically, the Commission ordered BNG and BGE to operate from physically separate locations and prohibited shared sales leads and joint calls. Finally, the Commission found that while promotional material may allow BNG to be identified as an affiliate of BGE, neither BGE nor an affiliate may represent that any advantage accrues to customers or others in the use of BGE services as a result of that customer or others dealing with the affiliate.

More recently, in Case No. 8677, the Commission initiated an investigation of the promotional practices of gas and electric companies to consider regulatory changes. In 1998, a Hearing Examiner issued a Proposed Order noting that significant changes, including restructuring, were taking place in these industries. Accordingly, the Hearing Examiner determined that many positions taken by the parties in Case No. 8677 had been superseded by changes in Commission policy or legislation, which rendered moot many of the parties' comments and recommendations. Therefore, the Proposed Order recommended closing that case. The Commission concluded that it was appropriate to consider promotional practice issues in the overall context of restructuring the utility industry. Thus, Case No. 8677 has been closed and issues involving utility promotional practices will be addressed herein.

On February 23, 1998, the Commission issued Order No. 74038 addressing transactions and standards of conduct for affiliates in its generic gas and electric proceeding in Case No. 8747. As discussed in more detail below, the Commission adopted 14 standards of conduct therein that apply to "core" gas and electric affiliates of all regulated utilities and four standards of conduct that apply to "non-core" affiliates.[7] The Commission in that case also agreed to extend the four cost allocation principles from Case No. 8577 to all gas and electric utility businesses with unregulated affiliates. In light of the mandates contained in the recently adopted Act and other statutory requirements, the Commission is revisiting these issues in conjunction with other restructuring proceedings.

The parties to this proceeding generally fall into three distinct groups: (a) the utilities; (b) potential competitive energy suppliers or marketers ("marketers"); and (c) regulatory/consumer advocates. The utilities advocate a restrained regulatory approach in this case, citing the advent of competition in their industry. Generally, they support a continuation of the affiliated activities standards and codes of conduct set forth in the Commission's 1998 decision in Case No. 8747. In addition, the electric utilities support the individual codes of conduct recently adopted in their restructuring proceedings.[8] In particular, the utilities claim that compliance reporting requirements are unnecessary and unfairly burdensome. They also take the position that broader disclaimers are generally unnecessary since any misconduct is governed by existing codes. Application of different standards of conduct should be based upon the services provided, they say. The utilities conclude that the standards adopted in Case No. 8747 and the settlement codes are sufficient and consistent with the Act and therefore, no further revisions or modifications are needed.

On the other hand, marketers support strict regulation of Maryland utilities and their affiliates, citing the perceived competitive advantages local utilities hold. Marketers

[7] In Case No. 8747, the term "core" service affiliate referred to affiliates engaged in activities previously provided by a utility as monopoly services (e.g., gas or electric marketing). "Non-core" services referred to all other services provided by the affiliates of utilities.
[8] See Case Nos. 8794, 8795, 8796 and 8797.

generally recommend complete separation (locational, operational, personnel, financial, etc.) of the utility from all affiliates, and they support applying an extensive list of additional standards. Marketers also recommend that the transfer of assets, in particular electric generation assets, should be made at fair market value.

Staff's comments in this proceeding have generally been consistent with the policies of the Commission set forth in Case Nos. 8577, 8709, and 8747. OPC generally favors the positions advocated by marketers. OPC strongly supports full separation of all utility affiliates and a prohibition of the use of the utility's name and logo by an affiliate. A pre-hearing conference was held in this case on August 16, 1999. On September 10, 1999, the Commission adopted a list of 18 issues and directed the parties to file comments on these issues as provided in Order No. 75381.[9]

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[9] The issues are as follows:

- What standard(s) of conduct should govern the interaction between a utility and its affiliates?
- Should there be different standards of conduct depending on whether an affiliate provides "core" or "non-core" services?
- If an affiliate provides both "core" and "non-core" services, which standard(s) of conduct should apply?
- Should different standards of conduct apply to a regulated utility and its GENCO than to other regulated utilities and their unregulated affiliates?
- Should a utility's affiliate(s) be permitted to engage in the generation of electricity within the utility's distribution territory?
- Should the Commission establish a code of conduct regulating interactions between affiliates conducting separate activities where both activities have been deregulated?
- What value should be used when utility assets or affiliated assets are sold or transferred between the companies (book or fair market value)?
- What constitutes a "utility asset"?
- What specific rules and procedures should the Commission adopt governing the sharing of employees and/or services between the utility and its affiliate?
- What reporting requirements should be developed to demonstrate utilities are in compliance with the standards of conduct?

(continued)

The September 10, 1999 directive also determined that municipal utilities should be excluded from this proceeding and that discovery would not be necessary since this is a generic proceeding. Further, the Commission determined that pending the decision in this case, Order No. 74038 in Case No. 8747 should remain in effect.

The parties filed Initial Comments on October 1, 1999. Reply Comments were filed October 26, 1999. The Commission held hearings in this matter from November 15 through November 19, 1999. Post-hearing Comments were filed December 10, 1999.

II. STANDARDS OF REVIEW

A. PSC Statutory Authority

It is well settled that the Commission has broad discretionary powers to regulate traditional utility functions in Maryland. Section 2-112 of the PSC Law[10] provides that "the Commission has jurisdiction over each public service company that engages in or operates a utility business in the State" and that it "has the implied and incidental powers

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- When should the details of utility's proposed promotion be filed with the Commission?
- What requirements should govern marketing of standard offer service for utilities and their affiliates?
- What disclaimers should be provided to detail the relationship between a utility and its affiliate or between an affiliate and parent?
- Should the Commission's Promotional Practices Regulations, codified as Subtitle 40 of Title 20 of the Code of Maryland Regulations, be revised?
- How and to what extent, if any, should utilities and/or their affiliates be permitted to engage in promotional practices as currently defined to offer incentives, rebates, or other promotions, including but not limited to, demand-side management to encourage the use or sale of electricity in any form?
- What requirements and restrictions should govern the relationship between utilities and their affiliates in communications, marketing, and permissible promotional practices?
- What enforcement and penalty provisions should be developed by the Commission for violations relating to the Standards of Conduct?
- Should there be any differences in standards or practices between regulated companies that provide: 1) gas service; 2) electric service; and 3) combined electric and gas service?

[10] Public Utility Companies Article of the Annotated Code of Maryland ("the PSC Law")

needed or proper to carry out its functions." Section 2-113 of the PSC Law provides that the Commission shall "supervise and regulate" public service companies subject to its jurisdiction to "ensure their operation in the interest of the public," to "promote adequate, economical, and efficient delivery of utility services in the State without unjust discrimination," and to "enforce compliance with the requirements of law by public service companies, including requirements with respect to financial condition, capitalization, franchises, plant, manner of operation, rates and service."

In addition to these broad powers, the Act sets forth certain legislative policies designed to facilitate the implementation of electric customer choice. Many of the provisions of the Act relate directly to utility/affiliate interactions. In particular, the Act requires the Commission to: ensure creation of competitive electric markets with appropriate customer safeguards; adopt appropriate codes of conduct; develop policies against discrimination; adopt complaint and enforcement procedures; and develop appropriate separation requirements.[11] This is consistent with Commission policies and initiatives in recent years. Specifically § 7-505(b) (10) provides:

> (i) On or before July 1, 2000, the Commission shall issue orders or adopt regulations reasonably designed to ensure the creation of competitive electricity supply and electricity supply services markets, with appropriate customer safeguards.(ii) On or before July 1, 2000, the Commission shall require:1. an appropriate code of conduct between the electric company and an affiliate providing electricity supply and electricity supply services in the State;2. access by electricity suppliers and customers to the electric company's transmission and distribution system on a nondiscriminatory basis; 3. appropriate complaint and enforcement procedures; and 4. any other safeguards deemed necessary by the Commission to ensure the creation and maintenance of a competitive electricity supply and electricity supply services market. (iii) On or before July 1, 2000, the Commission shall require, among

[11] Section 7-505 (b)(10)

> other factors, functional, operational, structural, or legal separation between the electric company's regulated businesses and its non-regulated businesses or non-regulated affiliates.

In addition, § 7-505(b)(3) requires the Commission to order electric companies to adopt policies and practices reasonably designed to prevent:

> (i) discrimination against a person, locality, or particular class of service or give undue or unreasonable preference in favor of the electric company's own electricity supply, other services, divisions, or affiliates, if any; and(ii) any other forms of self-dealing or practices that could result in non-competitive electricity prices to customers.

The Act also contains other important provisions relevant to this proceeding. The Act requires the Commission to establish rules regarding appropriate marketing and trade practices.[12] Section 7-505(b)(7) states that "[A]n electricity supplier may not engage in marketing, advertising, or trade practices that are unfair, false, misleading, or deceptive." Further, the Act provides that:

> (i) An electric company shall comply with all requirementsof the Commission in conducting regulated operations in compliance with this article.(ii) The Commission shall require each electric company to adopt a code of conduct to be approved by the Commission by a date to be determined by the Commission to prevent regulated service customers from subsidizing the services of unregulated businesses or affiliates of the electric company.[13]

Finally, the Act requires the Commission to "adopt regulations or issue orders to: (1) protect consumers, electric companies and electricity suppliers from anticompetitive and abusive practices;…and (7) establish procedures for dispute resolution."[14]

Section 7-506(b) requires electric companies to provide distribution services in their distribution territories to all customers and electricity suppliers on rates, terms of

[12] Section 7-505(b)(7)
[13] Section 7-505(b)(13)
[14] Section 7-507(e)(1) and (7)

access, and conditions that are comparable to the electric company's own use of its distribution system. In addition, electric companies shall connect customers and deliver electricity on behalf of electricity suppliers consistent with the PSC Law.[15] These provisions are consistent with Commission policies adopted for the competitive provision of natural gas services. Non-discrimination in the provision of gas and electric services and access to monopoly distribution systems by competitive suppliers is a fundamental Commission requirement to implement competition in these markets.

Section 7-507(e)(1) directs the Commission to adopt regulations or issue orders to protect consumers, electric companies, and electricity suppliers from anti-competitive and abusive practices. The Commission is also directed to require each electricity supplier to provide adequate and accurate customer information to enable customers to make informed choices regarding the purchase of any electricity services offered by the electricity supplier.[16] The Commission is also required to establish appropriate procedures for dispute resolution.[17]

Similarly, the Gas Act requires the Commission to adopt consumer protection orders or regulations for gas suppliers that: "(1) protect consumers from discriminatory, unfair, deceptive, and anticompetitive acts and practices in the marketing, selling, or distributing of natural gas, [and] (2) provide for contracting, enrollment, and billing practices and procedures . . ."[18]

This Order complies with the above legislative mandates and along with others issued during the restructuring proceedings, is designed to promote fully the creation of

[15] Section 7-506(d).
[16] Section 7-507(e)(2).
[17] Section 7-507(e)(7).
[18] Gas Act, § 7-604(a). The statute provides that the protections for gas and electric customers should be consistent, one with the other and that the requirements imposed on gas and electric suppliers should also be consistent.

competitive energy markets while ensuring appropriate customer safeguards and utility financial integrity. Building upon recent Commission decisions, this Order expands necessary codes of conduct applicable to gas and electric companies and their affiliates. Furthermore, as detailed herein, the Commission requires these companies to implement rules designed to ensure an appropriate degree of separation to reduce cross-subsidization and protect ratepayers. In addition, this Order requires electric and gas companies to adopt policies and practices designed to prevent discrimination or undue preferences in favor of their own supply, other services, divisions or affiliates and any other forms of self-dealing that could result in noncompetitive prices to customers.[19] This Order details marketing, advertising and trade practices that unfairly permit an affiliate to exploit its relationship with an electric or gas company and prohibits such conduct.[20] Electric and gas companies are hereby ordered to comply with all requirements of the Commission and to conduct their operations in compliance with the PSC Law. They are further required to adopt codes of conduct to be approved by the Commission as set forth herein to prevent regulated service customers from subsidizing the services of unregulated affiliates of the electric or gas company.[21]

B. Case No. 8747 Standards

This proceeding provides for an extension of the Commission's 1998 Order in Case No. 8747, which established standards of conduct for utilities and their affiliates. Therefore, a detailed discussion of that Order is appropriate. In Case No. 8747, the Commission concluded that the PSC Law provides the Commission with the authority to, among other things, adopt certain standards of conduct to ensure non-discriminatory

[19] Section 7-505(b)(3)
[20] Section 7-505(b)(7).
[21] Section 7-505(b)(13).

access to a utility's monopoly distribution system, to regulate the dissemination of certain information to affiliates, and to protect regulated utility customers. Two sets of standards were adopted in Case No. 8747, one for core-service related affiliates and another for non-core service affiliates.

In addition, the Commission found that certain cost allocation methodologies would prevent ratepayers from subsidizing the activities of utility affiliates. The four cost allocation principles applied to BGE's affiliate activities in Case No. 8577 (noted above) were adopted for all gas and electric companies that have unregulated business activities. The Commission also determined that it should be informed of all new non-regulated activities on a time-concurrent basis to allow the Commission to determine whether non-utility activities affect regulated services and allow it to ensure the protection of utility services and their customers.

The Commission stated that utilities could guarantee the indebtedness of an affiliate but that if such guarantee has a negative impact on a utility's credit rating, shareholders would be held accountable. Therefore, the Commission determined that, upon its approval, utilities would be permitted to lend money to affiliates at rates that the affiliate could obtain in the open market, thereby avoiding certain transaction costs. Quarterly earnings reports and appropriate cost allocation affidavits were mandated. The Commission emphatically stated that all start-up costs for affiliates should be supported by stockholders.

The Commission also adopted a standard to prohibit utilities from disclosing to their core service affiliates any information obtained in connection with providing regulated utility services to marketers or their customers. Additionally, any information provided by a utility to its energy marketing affiliates related to the utility's system, the marketing or sale of energy, or the delivery of energy was required to be made available contemporaneously to all non-affiliated energy suppliers. Of particular importance, the Commission determined in Case No. 8747 that an affiliate may use the utility's name or logo, but that neither may represent that an advantage accrues as a result of dealing with the affiliate. However, the Commission clearly ordered that there must be a prominently displayed disclaimer, which states that the utility and affiliate are separate entities. The Commission also decided that a complete prohibition on utility/affiliate transactions would be inappropriate. Finally, the Commission determined that the management and operational principles and policies adopted in Case No. 8709 should be embodied in standards of conduct set forth therein.[22]

In resolving the many issues raised in this case regarding affiliate relations with their regulated utilities, the Commission is guided by the precedents established in prior cases and by the extensive directives found in the Act. Some parties advocated lessening oversight standards while others would have us adopt strict separation standards. The regulatory mission to protect ratepayers, ensure just and reasonable rates, and maintain the financial integrity of the regulated entity in order to assure a safe, reliable system for the provision of gas and electricity guides the decisions in this case. The Commission will be monitoring the implementation of these standards very carefully and will enforce them strictly.

III. GENERAL POSITIONS OF THE PARTIES

In this generic proceeding, the Commission solicited the views of interested parties concerning the overall framework for affiliate standards of conduct. Numerous parties responded with detailed recommendations. Generally, the utilities endorse a

[22] Although the Commission did not order full structural separation in either Case No. 8577 or Case No. 8709, in the latter proceeding, the Commission did direct that the operational and managerial personnel of

continuation of the standards promulgated in Case No. 8747, but consistent with recent electric restructuring settlements. Delmarva Power and Light Company, d/b/a Conectiv Power Delivery ("Conectiv")[23] stated that three principles should be adopted in this case. Standards of conduct should prevent cross-subsidization, allow free markets to operate, and protect customers rather than competitors.[24] In addition, standards should differentiate between core and non-core affiliates.[25] Conectiv stated that core standards should be "strictly limited" to the retail energy marketing affiliate that competes with the jurisdictional service of the affiliated utility within that utility's franchised distribution service territory. Baltimore Gas and Electric Company ("BGE")[26], Potomac Electric Power Company ("Pepco")[27], and The Potomac Edison Company, d/b/a Allegheny Power ("APS")[28] all express support for the standards developed in Case No. 8747, as modified by their electric restructuring settlements.[29] BGE stated that the proponents of change should be required to make a clear case for any changes from the 8747 standards and that the Commission should honor the recently adopted standards in its settlement. Pepco stated that there is no need for new standards which will only undermine the efficient operation of the marketplace by providing artificial advantages to out-of-state competitors.

BGE's unregulated energy marketing affiliate be separate from BGE's utility operations personnel.

[23] The written comments filed by Conectiv are at docket numbers 53, 74 and 97. Conectiv also filed Joint Final Comments with BGE at Docket No. 102.

[24] Docket No. 53.

[25] In Case No. 8747, the Commission drew a distinction between core operations of affiliates – "those activities which duplicate or replace the essential services formerly provided only by a utility," and non-core activities – "those activities which are unrelated to the utility company's primary function." Order No. 74038, 89 MD PSC 54, 66 (1998). The Commission has also stated that transactions are core-service related if the affiliate engages in "activities previously provided by a utility as a monopoly service." *Id*. at 76.

[26] BGE's written comments are at docket numbers 57, 79 and 102. BGE also filed Joint Final Comments with Conectiv at Docket No. 102.

[27] Pepco's written comments are at docket numbers 64, 83 and 106.

[28] The written comments of APS are at docket numbers 46, and 96.

[29] The electric restructuring settlements are case numbers: 8794/8804 BGE, 8795 (Delmarva) Conectiv, 8796 Pepco, and 8797 (PE) APS.

The gas utilities in this proceeding generally support the principles espoused by the electric utilities. However, NUI Corporation ("NUI")[30] and Chesapeake Utilities Corporation, Maryland Division ("Chesapeake")[31] emphasize that a generic code of conduct is inappropriate[32] because the Commission should not impose the same standards for affiliate transactions and standards of conduct on all utilities.[33] NUI and Chesapeake note that due to their smaller size, their regulated utility customers in Maryland benefit from being part of a larger organization.

Washington Gas Light Company ("WGL")[34] and Columbia Gas of Maryland, Inc. ("Columbia")[35] also support the standards adopted in Case No. 8747. WGL argued that these standards reflect a balance for natural gas and other non-electricity marketing affiliates which adequately protects ratepayers without unduly restricting Maryland public service companies. WGL submitted that four goals must be met: no subsidies to affiliates, no undue preferences, a level playing field for all, and appropriate standards to protect consumers, not competitors. Columbia stated that a code should require utilities to offer services on a non-discriminatory basis, require that if confidential customer information is made available that it be available to all suppliers under similar terms, only permit a utility to engage in joint promotional activities with affiliates if such opportunities are available to all marketers on a non-discriminatory basis, and prohibit utilities from promoting any particular energy supplier. Columbia concludes that the

[30] NUI's written comments are at docket numbers 69. NUI does business in Maryland through an operating division now known as NUI Elkton Gas.
[31] Chesapeake's written comments are at docket numbers 54, 75 and 100. The natural gas transmission segment of Chesapeake's business is conducted through its wholly owned subsidiary, Eastern Shore Natural Gas. Eastern Shore's activities are regulated by the FERC, according to Chesapeake.
[32] NUI, Docket No. 69 at 3.
[33] Chesapeake, Docket No. 54 at 3.
[34] WGL's written comments are at docket numbers 55, 80 and 101.
[35] Colombia's written comments are at docket numbers 49, 78 and 98.

8747 standards are more than adequate to accomplish the desired activities and that there are instances where the standards should be relaxed.

Choptank Electric Cooperative ("Choptank") has addressed the issues from the perspective of a local cooperative.[36] Choptank generally agrees with Staff that the standards applicable to the utility and non-core affiliates adopted in Case No. 8747 provide adequate protection for customers and the competitive market.[37] However, as for Standard Offer Service ("SOS"), Choptank noted that it has neither settled its stranded cost case nor agreed to any code of conduct adopted in the investor-owned electric restructuring cases.[38] Choptank emphasizes that "[C]ooperatives are treated differently under State of Maryland Law with regard to Standard Offer Service."[39] Section 7-510(c)(3)(i) of the Act provides that cooperatives may choose to continue providing SOS beyond July 1, 2003.[40] Since cooperatives may choose to continue providing SOS, Choptank concludes that it has been an oversight on Staff's part to conclude that the settlements in the investor-owned utility cases should form the basis for standards of conduct between the electric utility's distribution business and its SOS business during the transition.[41] "It is inappropriate for provisions that the four IOU's have agreed to in settlement to apply universally to all electric companies in this case."[42] Further, while Staff suggested that the core service standards from Case No. 8747 should apply to all other energy affiliates, Choptank stated that there should be at least two modifications.

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[36] Docket No. 70.
[37] *Id*. at 2.
[38] *Id*. at 2-3.
[39] *Id*. at 3.
[40] This is generally the termination date for investor-owned utilities to be required to provide SOS.
[41] Docket No. 70 at 2-3.
[42] *Id*. at 2.

As for sales leads,[43] Choptank stated that as a member owned utility, if a customer requests a joint sales call or enters into contracts with a utility and its affiliate, joint calls should be permitted because this is "good member service."[44] According to Choptank, if a customer requests information about competitive core-service providers,[45] to the extent a list of core-service competitors is provided (including affiliates), the Commission should be the one that evaluates the worthiness of the service quality of those on the list and maintains the list going forward.[46]

A number of intervenors either provide services which are competitive to services of a utility or an affiliate or are assessing Maryland's restructuring energy markets with an eye toward becoming competitors of the incumbent natural gas and electric utilities. These "marketers" include: the Air Conditioning Contractors of America – National Capital Chapter, Maryland Alliance for Fair Competition and the Mid-Atlantic Petroleum Distributors Association ("Alliance")[47]; the Mid-Atlantic Power Supply Association ("MAPSA")[48]; Maryland Natural Gas, Ltd., t/a Operators Energy Services, Inc. and Baltimore Steam Company, t/a Trigen-Baltimore Energy Corporation ("Joint Commenters")[49]; Enron Energy Services, Inc. and Statoil Energy, Inc. ("Enron/Statoil")[50] and the Mid-Atlantic Propane Gas Association ("PGA").[51] Generally the marketers propose a more stringent code of conduct than the standards adopted in Case No. 8747.

The Alliance submitted that standards based on separation should be adopted to ensure that monopoly utilities do not interfere in competitive markets by conveying

[43] Case No. 8747, Core Standard No. 6.
[44] Docket No. 70 at 4.
[45] Case No. 8747, Core Standard No. 7.
[46] Id.
[47] The written comments of the Alliance are at Docket Nos. 59, 87 and 108.
[48] The written comments of MAPSA are at Docket Nos. 63, 86 and 109.
[49] The written comments of the Joint Commenters are at Docket Nos. 61, 84 and 107.
[50] The written comments of Enron/Statoil are at Docket Nos. 60, 85 and 104.
[51] The written comments of PGA are at Docket No. 45.

substantial and irreproducible advantages upon their unregulated affiliates, and to ensure that ratepayers do not cross-subsidize the utilities' unregulated ventures.[52] The Alliance concludes that separation also renders much of the tracking, enforcement and dispute resolution procedures unnecessary.[53] The Alliance has proposed a code of conduct for Commission adoption.[54]

MAPSA recommends replacing the core/non-core distinction with a distinction between regulated utility services and unregulated activities. A code of conduct should also require physical and operational separation of the utility and affiliate with exceptions held to a minimum. All utility services should be provided on a non-discriminatory basis. MAPSA also contends that to the extent permitted, transfers of assets should be at least at fair market value. MAPSA opposes the sharing and non-permanent transfer of operational personnel as well as joint promotions and marketing. In addition, MAPSA asserted that a disclaimer should be required where the affiliate uses the name and logo of the utility. Finally, MAPSA advocates adoption of strict and expeditious compliance enforcement and requirements.

The Joint Commenters say that the unequal starting positions of potential competitors greatly complicates the transition to competition and that inertia may preserve the utility's dominant market share. The Joint Commenters say the Commission should adopt standards on non-discrimination, disclosures, information, and separation. Specifically, the utility should not disclose customer information to affiliates except where the customer consents to disclosure and the information is available to all competitors on a non-discriminatory basis. Affiliates should be prohibited from advertising their affiliation with utilities, or using utility names or logos. The Joint

[52] Alliance; Docket No. 59 at 4.
[53] Id.

Commenters emphasize that in order for these standards to be of benefit, they must be enforceable. Therefore, the Commission should require all exchanges between the utility and its affiliates to be made public unless the utility has, in advance, met its burden of proving that the public interest warrants exemption for a particular transaction or class of transactions. Further, the utility should establish a single gateway for all electronic interchange with its affiliates and publicly post the full prices, terms and conditions upon which it buys services from an affiliate or sells services to an affiliate. The Joint Commenters conclude that strict structural separation provides a more certain and easy method for controlling the abuse of market power than either cost accounting rules or reporting requirements.

Enron/Statoil submitted that anti-competitive conduct by utilities, such as discrimination in providing access to essential facilities, sharing of information with affiliates and cross-subsidization, must be prohibited if consumers are to see the benefits that come from competitive alternatives. Enron/Statoil concludes that the Case No. 8747 standards represent a good starting point. However, as a result of the Act and changes about to take place in the provision of energy services, certain additional standards and a degree of re-tooling of existing standards is required. Enron/Statoil submitted that physical and operational separation between the utility and all unregulated competitive affiliates will minimize inadvertent interaction and communications among personnel that should not be interacting. They believe that, to be meaningful, the distribution, generation, and marketing businesses must be separated from each other. In addition, during the transition period, there is a need for functional separation within the utility between merchant-related (i.e., Standard Offer Service) activities and wires-related

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[54] Docket No. 59, Appendix A.

activities. Once appropriate separation principles are established, Enron/Statoil asserted that standards must govern the conduct between these separate entities and draw bright lines between permissible and impermissible behavior.

To effectuate these goals, Enron/Statoil proposes a number of additions to the Case No. 8747 code of conduct. First, to ensure non-discrimination, Enron/Statoil suggested that a distribution company should be prohibited from providing preferential services to an affiliate, transmission service should be supplied only under the utility's FERC open access tariff and associated rules, and utilities should provide distribution service only under their Commission approved tariff. Second, Enron/Statoil advocates a prohibition on the promotion of SOS because as a default service, SOS is not intended to be a service that is marketed. Citing examples in Pennsylvania, Enron/Statoil said that if the incumbent utility is allowed to market SOS, then it will undermine the development of a competitive market. Third, they propose six modifications to the existing code to strengthen the protections against affiliate abuse. Generally, these proposals prohibit affiliates from representing that their service is superior, or that there is any benefit to a distribution customer by purchasing power from an affiliate. These rules are extended to gas and combination utilities as well. Finally, Enron/Statoil recommends disclaimers for affiliates, including that the affiliate is not regulated by the Commission. Enron/Statoil stated that name recognition for affiliates is at odds with competitive goals. Competition, they claim, is furthered only if affiliates are made to market and attract customers based on the quality and price of their own stand-alone services. If the use of common names and logos is not prohibited, however, Enron/Statoil recommends that the Commission require the affiliate to pay fair market value for such use.

The Mid-Atlantic Propane Gas Association generally favors separation, competitive procurement, no sharing of customer information or billing, and non-discriminatory services by utilities. Further, joint promotions with an affiliate should be permitted only if such promotions are made available to third parties under the same terms and conditions. PGA also argued that affiliates should be prohibited from claiming any advantage due to their relationship with the utility. Affiliates should be prohibited from using trade names or logos of the utility, but, an affiliate could identify itself as a subsidiary of a utility. Sales leads should be prohibited unless provided by the utility to all suppliers, with certain customer privacy protections. Transfers of assets, services or personnel should comply with a Cost Allocation Manual ("CAM") and be at market rates. Complaints should first be filed with the utility and then with the Commission if not resolved by the utility within 45 days. The Commission should audit and inspect utilities as necessary to enforce compliance according to the PGA.

The Office of People's Counsel ("OPC")[55] submitted extensive comments in this proceeding. OPC submitted that a code of conduct for affiliated businesses is important for two reasons: 1) to avoid cross-subsidies; and 2) to prevent affiliates from gaining an advantage in their retail market because of their affiliation to the regulated utility. OPC advocates complete separation of utility and affiliate activities, except for shared corporate services. According to OPC, clear separation of entities and names has an added advantage in that it makes enforcement of affiliate rules easier and less invasive. If any other employees are shared, asymmetric pricing (at the greater of market price or book value) should be used or fully allocated costs plus a 10% adder to cover unquantified costs and benefits. Utility assets, including intellectual property, should be

[55] OPC's written comments are at docket numbers 50, 77 and 103. OPC's testimony was prepared by William B. Marcus.

priced at the higher of cost or fair market value. Sharing of customer databases and billing systems should be prohibited unless offered to other market participants at the same cost. Joint marketing of utility and affiliate services should also be prohibited. Books and records should be available to the Commission and periodic audits performed to assure compliance with the standards. Affiliates should be financially separate to avoid adverse impacts on the utility or the utility should be compensated for loans and guarantees. The Commission should also adopt restrictions on utility dividend pay-outs that assure that the utility capital structure is maintained at a reasonable level and that the worthiness of the utility is not impaired by transfers to the holding company.

The Attorney General's Consumer Protection Division ("AG-CPD")[56] also participated in this case. According to AG-CPD, consumers must be able to make informed decisions based upon complete and accurate information regarding goods and services. Initially, AG-CPD stated that consumers need to know who is making the offer and the relationship of that entity to other companies participating in the electricity marketplace in order for consumers to make informed purchasing decisions.[57] In its Reply Comments, the AG-CPD stated that "[U]pon reflection, however, we realize that no amount of disclosure can overcome the misimpression given to consumers by an affiliate's use of its parent utility's name or logo in its advertising and promotional materials."[58] Since regulated utilities will operate separate and apart from their deregulated affiliates, the AG-CPD concludes that it would be inappropriate for these affiliates to use the name or logo of the utility.

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[56] The written comments of the AG-CPD are at docket numbers 52, 71 and 95.
[57] Docket No. 52 at 1.
[58] Docket No. 71 at 1

The Public Service Commission Staff ("Staff")[59] recommends that the core/non-core definitions that were adopted in Case No. 8747 be replaced with a broader model of affiliate relationships. Staff asserted that its model addresses changes in the industry that result from the Act and the electric utility stranded cost settlements. Staff recommends that utility/affiliate relationships be separated into four distinct categories. Staff's position is summarized as follows:

1) For the Regulated Electric Company (Electric Company) and all non-energy affiliates, Staff recommends the Standards of Conduct adopted in Case No. 8747 for non-core services, after making the language consistent with the Act.

2) For the Electric Company and the SOS provider, Staff recommends the generic version of the Standards of Conduct for SOS contained in the individual settlement agreements.

3) For the Electric Company and its GENCO affiliate, Staff recommends that during the transition period, the generic standards based on the individual settlement agreements for GENCOs should apply. Following the transition period, the GENCO should be fully structurally separated from the electric company, and that standards of conduct adopted for energy service affiliates in Case No. 8747, language corrected, should apply.

4) For the Electric Company (Gas Company) and all other Energy Supply affiliates, the Staff recommends the standards of conduct adopted for energy service affiliates in Case No. 8747, language corrected, should apply, as well as the Equal Access Standards developed in the settlements.[60]

With regard to these standards, Staff argued that the non-core standards applied to non-energy affiliates are all-inclusive, flexible, and avoid micro-management. According to Staff, the GENCO standards in the electric settlements are consistent with the Case No. 8747 standards and in addition, include necessary customer and market protections for the transition period. Therefore, Staff does not believe that additional generic standards need to be developed for gas company affiliate relationships or any other relevant person during the transition period. However, afterward the GENCO must be fully structurally

[59] Staff's written comments are at Docket Nos. 51, 73 and 105.
[60] Docket No. 51 at 15.

separated from the electric company in order to comply with the Act. This would also restrict any financial relationship between these affiliates such as loans or loan guarantees.

In conclusion, Staff argued that standards should be designed to protect customers from anti-competitive abuses, including equal access limitations, cross-subsidization, information asymmetries, and financial risks. However, standards should not, according to Staff, deny customers the benefits of efficiencies that can result from affiliate interaction, nor should the affiliate face unnecessary restrictions that could result in financial harm compared to their competitors.

IV. NEW STANDARDS OF CONDUCT

The Commission concludes that the standards of conduct for transactions between a utility and both core and non-core affiliates that were adopted in Case No. 8747 provide a good starting point, but should be modified. Those standards reflected appropriate decisions at that time. However, with the advent of electric generation competition, the expansion of the competitive gas programs, legislative changes, the many changes utilities are currently undergoing, and the compliance problems that may have arisen as a result of perceived ambiguities in the standards, it is necessary to revisit those standards. The new standards of conduct adopted in this case are based upon the record herein and are intended to foster the following important Commission goals to:

- prevent cross-subsidization of affiliates;
- prevent affiliates from gaining any improper advantage in their competitive markets because of their affiliation to the regulated entity;
- minimize inappropriate communication between the utility and affiliate regarding confidential information;
- protect the privacy of consumers; and

- prohibit discrimination in the provision of regulated services.

Some parties recommended that the Commission impose strict structural separation between utilities and all affiliates to advance these goals. Other parties suggested that the 8747 standards were sufficient to meet these goals and therefore, no changes were necessary. After analyzing the record in this case, the Commission has chosen a more moderate course than strict structural separation because it recognizes that certain economies of scale and scope can be beneficial to ratepayers. The Commission is aware that it must be vigilant in making sure that utilities and their affiliates do not overstep appropriate boundaries to disadvantage the ratepayers or harm the competitive markets. Furthermore, the Commission is mindful that compliance with the 8747 standards has been uneven at best. Consequently, the Commission has chosen to enhance the standards of conduct and broaden their applicability to non-core affiliate transactions in certain instances.

<u>Standards of Conduct for Utilities in Transactions With Core Service Affiliates</u>

1. Neither a utility nor its core service affiliate(s) shall represent that any advantage accrues to a customer or others in the use of utility services as a result of that customer or others dealing with the core service affiliate(s). Neither a utility nor its core service affiliate(s) shall represent that their affiliation allows the core service affiliate(s) to provide a service superior to that available from other suppliers.

2. Joint sales calls may not be initiated either by a utility or its core service affiliate(s) in order to avoid the appearance of favoritism. If a customer requests a joint sales call, joint calls may be conducted. If a customer enters into a contract with a core service affiliate, a joint call relating to that contract may be conducted.

3. Advertising material utilized by a core service affiliate of the utility may identify the core service affiliate's

association with the utility. If the core service affiliate identifies its association with the utility, then each advertisement must state that the core service affiliate is "not the same company as the utility" and that the core service affiliate's "prices are not set by the Maryland Public Service Commission." If core service affiliates share the name or logo of the utility, the core service affiliate(s) must state the above disclaimer in any advertising material.

4. Joint promotions, marketing, and advertising between a utility and its core service affiliate(s) are prohibited.

5. A utility and its core service affiliate(s) shall operate from physically separate locations to avoid the inadvertent sharing of information.

6. A utility must not provide sales leads to its core service affiliate(s). It must refrain from speaking for or appearing to speak on behalf of its core service affiliate(s).

7. If a customer requests information from the utility about competitive core services, to the extent the utility responds to the request, it shall provide a list of all similar providers of that core service on its system. It shall not highlight or promote its core service affiliate(s) in any way.

8. A utility must process all requests for service by any provider in the same manner and within the same period of time as it processes requests for service from its core service affiliate(s).

9. A utility must apply all the terms and conditions of its tariff and other tariff provisions related to delivery of energy services in the same manner, without regard to whether the supplier is a core service affiliate.

10. A utility may not condition or tie the provision of regulated utility services to any other product or service.

11. A utility may not give any preference to its core service affiliate(s) or customers of its core service affiliate(s) in providing regulated utility services. The utility shall treat all similarly situated providers and their customers in the same manner as the utility treats the core service affiliate or the core service affiliate's customers.

12. Except upon the informed consent of the customer, a utility may not disclose any customer-specific information obtained in connection with the provision of regulated utility services. This requirement does not apply to the extent a utility makes a disclosure that complies with the Commission's Consumer Protection Orders, Nos. 75949 and 76110.

13. A utility must contemporaneously disclose any information provided to its energy marketing affiliate(s) to all non-affiliated suppliers or potential non-affiliated suppliers on the system with respect to its system, the marketing or sale of energy to customers or potential customers, or the delivery of energy to or on its system. Disclosure of such information must be made by a posting on the general alert screen of the utility's electronic bulletin board.

14. A utility must offer the same discounts, rebates, fee waivers, penalty waivers or other special provisions to all similarly situated non-affiliated suppliers or customers that it may offer its affiliate or customers of its affiliate. The utility must make such contemporaneous offers by making an appropriate posting on the general alert screen of its electronic bulletin board, or by some other appropriate fashion which insures an equal ability and time to utilize such offering.

Standards of Conduct for Utilities in Transactions
With Non-Core Service Affiliates

1. Neither a utility nor its non-core service affiliate(s) shall represent that any advantage accrues to a customer or others in the use of utility services as a result of that customer or others dealing with the non-core service affiliate(s). Neither a utility nor its non-core service affiliate(s) shall represent that their affiliation allows the non core service affiliate(s) to provide a service superior to that available from other suppliers.

2. A utility may not give any preference to its non-core service affiliate(s) or customers of its non-core service affiliate(s) in providing regulated utility services. The utility shall treat all similarly situated providers and their customers in the same manner as the utility treats the non-core service affiliate or the non-core service affiliate's customers.

3. Advertising material utilized by a non-core service affiliate of the utility may identify the non-core service affiliate's association with the utility. If the non-core service affiliate identifies its association with the utility, then each advertisement must state that the non-core service affiliate is "not the same company as the utility." If non-core service affiliates share the name or logo of the utility, the non-core service affiliate(s) must state the above disclaimer in any advertising material.

4. A utility may not condition or tie the provision of regulated utility services to any other product or service.

5. Joint promotions, marketing and advertising between a utility and its non-core service affiliate(s) are prohibited.

6. Except upon the informed consent of the customer, a utility may not disclose any customer-specific information obtained in connection with the provision of regulated utility services. This requirement does not apply to the extent a utility

makes a disclosure that complies with the Commission's Consumer Protection Orders, Nos. 75949 and 76110.

7. A utility must offer the same discounts, rebates, fee waivers, or penalty waivers or other special provisions to all similarly situated non-affiliated suppliers or customers that it may offer its affiliate or customers of its non-core service affiliate.

Core and Non-Core Standards No. 1 have been modified to clarify the Commission's policy prohibiting any representation or suggestion that the relationship between a utility and its affiliate allows the affiliate to provide a service that is superior to competitors. These standards further prohibit any representation or suggestion that an advantage accrues to a customer in the use of utility services as a result of dealing with the affiliate. This broad general non-discrimination provision reflects longstanding Commission policy and legal requirements, particularly § 7-505(b)(3).

Core Standard No. 2 prohibits joint sales calls because the Commission wants to prevent utilities from favoring their affiliates in ways that could be detrimental to the development of competitive markets. Moreover, the modifications to this standard clarify that the Commission will only permit joint sales calls upon the request of a customer. However, it does not prevent joint calls once a contract has been entered into between an affiliate and a customer.

Core and Non-Core Standard No. 3 continues to permit an affiliate to identify its association with a utility in its advertising materials. However, the Commission will now require appropriate disclaimers to protect the public from confusion. This is a modification to our previous standard because the Commission believes it is important that customers clearly understand that they are not dealing with the utility. The core standard has an additional disclaimer that requires affiliates to notify customers that the affiliate's services, which generally were formerly regulated monopoly services, are not subject to price regulation by the Commission.

Core Standard Number 4 implements a complete ban on joint promotions with a core affiliate.[61] This is a modification to the previous standard adopted in Case No. 8747 which permitted such promotions, provided such promotions were offered to all other core service competitors upon the same terms and conditions. This prohibition is extended to marketing and advertising practices as well. The Commission concludes that it is not the role of utilities and their ratepayers to promote or market the activities of affiliates. Affiliates should succeed or fail as a result of their own efforts. Lastly, the prohibition is made applicable to transactions with non-core affiliates in Non-Core Standard No. 5 because the Commission's concerns regarding cross-subsidization and a competitive marketplace are not limited to utility transactions with core affiliates. Consequently, use of the utilities' billing envelope for affiliate marketing materials is prohibited for both core and non-core affiliates.

Additionally, some of the parties to this proceeding requested clarification on whether certain specific joint promotional or marketing practices are prohibited by the Commission's codes of conduct. Several parties have asked whether the following practices are permissible: shared booths at a fair or trade show; T-shirts or other personal items indicating the names of both a utility and an affiliate; joint web sites as well as "hyperlinks" from a utility's web site to an affiliate's; and references or access to an

[61] Joint promotions do not include billing. The Commission has previously addressed billing for electric and gas supply, which permits all marketers (both affiliate and non-affiliates) to use the utility's bill for consolidated billing. A non-core affiliate may use the utility's bill to bill for its services.

affiliate through a utility's call center. The Commission hereby declares that all of these efforts at joint marketing, advertising and promotions which inappropriately link corporate efforts to market their sales and services are specifically prohibited. This is because these references would create an inappropriate benefit for an affiliate in the newly competitive markets. In addition, misrepresentations of an affiliate's relationship with the utility would cause customers to be confused that the utility and an affiliate are the same company. Similarly, the Commission wishes to specifically note that an affiliate's use of the phrase, "the company you've known and trusted [for X years]" or, comparable phrases, are misleading because they falsely imply that the affiliate has a history of service and reliability that is co-extensive with the utility. Therefore, these representations are hereby prohibited.

Core Standard No. 5 requires a utility and a core affiliate to operate from separate locations. This protection is necessary to prevent the inadvertent sharing of market sensitive information and to promote and protect the competitive environment.

Core Standards No. 6, No. 7 and No. 11 as well as Non-Core Standard No. 2 reflect the need to prohibit utilities from bestowing undue advantages upon affiliates. This serves to safeguard competition and encourage marketers to offer their services in Maryland. New language has been added to clarify these prohibitions.

Core Standards No. 8, No. 9 and No. 13 are specific non-discrimination provisions. As the Commission has stated repeatedly, non-discrimination in the provision of regulated utility services is a hallmark of Commission policy. Utilities are to apply their tariffs evenhandedly.

Core Standard No. 10 and Non-Core Standard No. 4 reflect the fact that consumers should not be bound to purchase anything to receive natural gas or electric service. These consumer protection standards reflect long-standing Commission policy.

Core Standard No. 12 has been modified to reflect recent Commission decisions regarding the disclosure of confidential information. As the Commission stated in its recent consumer protection orders, utilities may sell customer lists (consisting of customer names, addresses and telephone numbers) upon the same terms to affiliates and non-affiliates, provided that the utility conspicuously discloses to affected customers that the utility intends to release customer lists and that customers may prevent disclosure upon request. The Act[62] also permits electric companies and suppliers to disclose a customer's billing, payment and credit information for bill collection and credit reporting purposes. In all other instances, except upon the informed consent of the customer, a utility may not disclose any customer-specific information obtained in connection with the provision of regulated utility services. The Commission finds that consumer confidentiality is such an important issue that the protections should be extended to transactions involving non-core affiliates. This is embodied in new Non-Core Standard No. 6.

Core Standard No. 14 requires utilities to offer the same rebates and other special promotions on a non-discriminatory basis. New Non-Core Standard No. 7 applies this rule to transactions with non-core affiliates because of the rapid changes taking place in the scope of affiliate activities and the need to prohibit utilities from bestowing undue benefits on these new affiliates. Furthermore, the Commission wishes to clarify that Core Standard No. 14 and Non-Core Standard No. 7 do not permit utilities to engage in joint

[62] Section 7-505(b)(6).

promotions, marketing or advertising in contravention of Core Standard No. 4 and new Non-Core Standard No. 5.

As a final matter, the Commission notes that municipal utilities and Eastern Shore Gas Company are exempt from this Order.[63] Furthermore, cooperatives and small utilities are covered by these standards of conduct and other rules set forth herein. However, because of their unique characteristics, cooperatives and small utilities may have these rules waived by the Commission if, upon request, the Commission determines that the rules are unduly burdensome. Finally, the parties are advised that the Commission may revisit some issues at the end of the electric restructuring transition period, if appropriate, or at an earlier date, if necessary.

V. ISSUES

A. Core and Non-Core Issues[64]

1. Parties' Positions

A key issue raised in these proceedings is the distinction between "core" and "non-core" services. The utilities generally accept the core/non-core distinction but emphasize that it is the nature of the services that is the distinguishing feature, not the affiliate itself. Dr. Kenneth Gordon, Senior Vice President of National Economic Research Associates, Inc. ("NERA") testified as a policy witness on behalf of several utility companies.[65] He stated that the purpose of standards of conduct covering distribution utilities and core affiliates is to prevent misuse of the distribution utility's control of essential facilities and to prevent subsidies of competitive energy suppliers by the utilities. Essential facilities, Dr. Gordon argued, are not involved in non-core

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[63] Order does not apply to Municipalities and ESGC.
[64] This section deals with Issue No. 2: Should there be different standards of conduct depending on whether an affiliate provides "core" or "non-core" services? and Issue No. 3: If an affiliate provides both "core" and "non-core" services, which standard(s) of conduct should apply?

activities. Therefore, he concludes that it is appropriate to exclude non-core affiliate activities from standards of conduct designed for core service affiliates. In addition, he takes the position that, absent demonstration that non-core activities involve cross-subsidization or discriminatory transfers of public utility services, products or information, then the Commission should not be concerned with the activities of non-energy affiliates. Dr. Gordon submitted that consumers benefit when utilities compete in non-energy markets. Dr. Gordon concludes that "[T]he application of the standards of conduct to the activities of non-energy affiliates is unnecessary and would only serve to artificially limit the competition faced by firms in those non-core, non-utility markets."[66] Conectiv noted that the non-core markets in which Conectiv and its affiliates in Maryland compete are generally "fully mature, vigorously competitive markets." The utility and its affiliates are the new entrants and as such, do not pose any threat of monopolizing any one of the existing markets.[67] Pepco also recommends eliminating entirely the regulations governing utilities and non-core service affiliates. According to Pepco, "Maryland utilities enjoy no special advantages in the provision of 'non-core' services and should not be handicapped in their efforts to build businesses in 'non-core' areas."[68]

The utilities also take the position that the Commission should avoid imposing the strictest code of conduct on all activities of the "hybrid" affiliate which is an affiliate that provides both core and non-core services. According to Pepco, "[T]he standards of conduct should apply on the basis of the type of service being provided by the affiliate."[69] WGL, Columbia and Chesapeake agree.[70] BGE stated that "an across-the-board

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[65] Dr. Gordon's testimony was sponsored by BGE, Conectiv, Columbia, Pepco and APS.
[66] Docket No. 56 at p. 14.
[67] Docket No. 53 at p. 13-14.
[68] Docket No. 64, Attachment A, p. 1.
[69] Docket No. 64, Attachment A, at 1 - 2.
[70] Docket No. 55, Appendix A, at 2; Docket No. 49 at 3; and Docket No. 54.

application" of the core standards "may only lead to the creation of additional affiliated companies in order to achieve compliance."[71] Conectiv submitted that as a general rule, the core standards should be applied only to energy transactions engaged in by the affiliate within the utility's regulated service territory.[72]

The marketers take a much different position. Generally, they recommend a single code of conduct, which is more stringent then what the utilities proposed. The Alliance argued that "[T]here should be no distinction in the standards of conduct that apply to the relationship of the utility and the affiliate regardless of the services provided by the affiliate."[73] According to Enron/Statoil, "[A]ll services provided by distribution companies are core in nature, and it is appropriate for a single set of standards to govern all behavior of the monopoly utility with regard to its affiliates."[74] The Joint Commenters say that there is not any single bright line test and "[B]asing different codes of conduct on a distinction between core and non-core services places too much pressure on the determination of the core vs. non-core nature of an affiliate's activities."[75] However, if there are to be two sets of standards, the marketers advocate application of the core service standards to hybrid affiliates. According to the Alliance, "by applying the most stringent standards that are applicable to any one component of the business to the entire business, the Commission will ensure that business is not able to use less stringent standards to gain a competitive advantage in the market."[76]

MAPSA argued that, in light of the evolution of the energy services markets, the Commission should disregard the core/non-core services distinction and focus instead

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[71] Docket No. 57 at 5.
[72] Docket No. 53 at 14.
[73] Docket No. 59 at p. 5.
[74] Docket No. 60 at p. 16.
[75] Docket No. 61 at p. 9.
[76] Docket No. 59 at 8.

upon the distinction between the regulated services of the utility and any unregulated activities. If any distinction beyond this is necessary, then it should be based upon an affiliate's provision of energy-related (i.e., traditional utility services) or non-energy-related activities.[77]

OPC emphasizes that a core vs. non-core distinction should not be related as much to the energy-related nature of the business as to the type and location of products being sold."[78] OPC suggested that evidence indicates that utility name recognition is very low outside the utility's service territory. "If there is a differentiation in applicability of standards, more stringent standards would be necessary for "core" products and services, marketed in the utility's territory."[79] OPC asserted that issues of self-dealing, unfair competition and market power are more likely to apply to mass-marketed retail unregulated activities that target the utility's customers. Consequently, more stringent requirements are necessary for affiliates that target the utility's native customers.[80] OPC concludes that, "[I]f a single affiliate provides both core and non-core services, the core service code of conduct should apply to that affiliate."[81]

Staff has recommended replacing the core/non-core distinction with a four-part model of affiliate relationships that reflects the changes in the industry as a result of the passage of new legislation and the settlements of the stranded cost cases.[82] Staff also noted that the electric company's power marketing affiliates are currently providing both core and non-core services. According to Staff, during the transition period, the generic

[77] Docket No. 63 at p. 6.
[78] Docket No. 50 at p. 12.
[79] *Id*.
[80] *Id*.
[81] *Id*. at 14.
[82] Docket No. 51 at p. 15.

settlement standards are adequate for hybrid affiliates. After the transition period, Staff supports application of the core service standards to hybrid affiliates.

2. Commission Decision

In Case No. 8747, the Commission observed that "[m]oving from monopoly providers to provider choice introduces complexities not in existence" before.[83] The Commission stated:

> The standards of conduct which we adopt today will put all participants in these emerging markets on notice as to those things which a utility may and may not do in interactions/transactions with its energy affiliates. Thus, in addition to protecting customers of the regulated utility, our interest in prescribing these standards of conduct is to facilitate the growth of competitive markets in the retail sale of gas and electricity. If such markets can be achieved, consumers should benefit through lower prices and expanded choices for these services.
>
> From the standards of conduct to be applied to a utility's energy affiliates, we adopt a more limited set of standards to be applied to affiliate activities unrelated to the core utility business. For non-core service affiliates, our interest extends to standards necessary to assure just and reasonable rates for and the adequate provision of regulated utility services and to protect against the preferential provision of utility services.[84]

The Commission then adopted four non-core affiliate standards of conduct and 14 core-service affiliate standards in Case No. 8747.

The Commission is mindful of the rapid changes taking place in the energy marketplace. Some parties have advocated standards based upon energy or non-energy affiliate relationships. Others have suggested that one set of standards should apply to all affiliate relationships. Multiple variants have been suggested by a few parties. However, the Commission finds that the core/non-core standards reflect the fact that important

[83] Case No. 8747, Order No. 74038, 89 MD PSC 54 , 67 (1998).
[84] *Id*. at p. 19-20.

distinctions exist between various types of utility/affiliate transactions. Furthermore, these standards have been tailored to prevent cross-subsidization of affiliates by utilities, minimize any anti-competitive conduct as a result of transactions between utilities and their affiliates and to preserve the confidentiality of certain information and data. Upon analysis, the Commission concludes that the basic core/non-core framework continues to be appropriate and will be retained for the affiliate standards of conduct.

The Commission has also stated that "jurisdiction over a utility's unregulated activities exists to the extent 'necessary to assure just and reasonable rates for and the adequate provision of regulated utility services.'"[85] In addition:

> The Commission's regulatory authority extends to public utility <u>services</u>. "Public utility services" are limited to those services which a utility company provides under the privileges granted to it by the State. Thus, the Commission's jurisdictional powers permit us to regulate ancillary or miscellaneous business activities related to a company's franchise rights and duties to provide utility service. Further, the Commission regulates those practices and services that have a sufficient nexus to the utility company's status as a public utility.[86] (emphasis added)

Furthermore, as a result of passage of the Natural Gas Act, the Legislature has clarified the Commission's authority and jurisdiction over gas companies and gas suppliers. Generally, this authority is consistent with the Commission's present authority over electric companies and electric suppliers. Therefore, this Order will apply to all gas and electric utilities in Maryland, and all core affiliates. This Order extends to non-core affiliates to the extent necessary to protect regulated services, the financial integrity of regulated entities, and to avoid cross-subsidization.

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[85] *Id*.
[86] Case No. 8577, Order No. 72107, 86 MD PSC 225, 230 (1995).

For purposes of clarification, the Commission finds that core services of a gas utility include the provision of electric service and core services of an electric company include the provision of gas service. This clarification avoids the incongruous result of stricter treatment of a combination gas and electric utility compared with a gas only or electric only utility. Therefore, all affiliates that provide essential gas or electric services will be deemed "core affiliates."

Furthermore, the Commission also finds that the core standards of conduct will be applicable to all activities of an affiliate that provides any core services. An affiliate that provides both core and non-core services can avoid application of the core standards by establishing a separate non-core affiliate. The Commission reiterates its previous findings that the core standards of conduct will be applicable to all activities of an affiliate that provide any core services.

B. Gas, Electric and Combination Utilities[87]

1. Parties' Positions

There was some discussion in this proceeding about whether distinctions should be recognized for gas, electric, and combined gas and electric companies based upon the type of energy service they provide. The utility companies generally agreed with Pepco's position that the codes of conduct "should be equally applicable to all regulated entities in order to ensure that none receive a competitive advantage."[88] BGE suggested that the standards adopted should also reflect the principles approved in its restructuring settlement.[89] APS concurred with BGE.[90]

[87] This section responds to Issue No. 18: Should there be any differences in standards or practices between regulated companies that provide: 1) gas service; 2) electric service; and 3) combined electric and gas service?
[88] Docket No. 64, Attachment A at 6.
[89] Docket No. 57 at 8.
[90] Docket No. 46 at 5.

WGL suggested that the Commission should be cognizant of the differences in electric and gas restructuring. "The obvious difference is that competition for natural gas commodity is at a very mature stage."[91] In addition, there are physical differences. Historically, electricity used in Maryland has been generated near service territories, which has had a tremendous impact on resolving transmission constraints.[92] In addition, electricity cannot generally be stored on an economic basis. WGL argues that the "absence of storage capability of electricity has rather natural implications for pricing as well as potential opportunities for market manipulation."[93] The ability to store gas mitigates market power because of the supply enhancement capability during peak periods.[94]

Chesapeake emphasized that the Commission "should take into account the unique aspects of the individual utility involved such as the utility service territory, the size of the utility, and the market share and power of the utility."[95] Consequently, Chesapeake does believe there should be different standards for gas, electric, and combination utilities.[96] Chesapeake argues that, "[T]he reason for establishing any standards of conduct should be to address real problems, not require a company to abide by a set of rules when the underlying problems do not exist for that company."[97]

The marketers advocate a single generic code of conduct.[98] The Alliance argued that a separate GENCO code of conduct might be an exception.[99] Enron/Statoil noted that while there are differences in the commodity and operations, "the same economic

[91] Docket No. 55, Appendix A at 7.
[92] *Id*.
[93] *Id*. at 8.
[94] *Id*.
[95] Docket No. 54.
[96] *Id*.
[97] *Id*.
[98] Docket No. 62 at 28, Docket No. 60 at 28, Docket No. 59 at 23.
[99] Docket No. 59 at 23.

incentive exists for a distribution company, gas or electric, to favor a transaction that benefits the corporate group of which it is part."[100] Enron/Statoil also argued that the adoption of electric restructuring settlements "does not eliminate the need for a comprehensive code of conduct to be developed in this proceeding for generic application to all utilities in the State."[101] The Joint Commenters say that the Commission may wish to consider particular provisions that would apply to a combination utility. They claim that the "potential for fuel substitution creates unique competitive issues where a utility provides combined electric and gas service."[102] The Joint Commenters suggest that the Commission consider a more stringent code for combination utilities in a separate proceeding.[103] At the very least, they say, core service standards should apply to all transactions between the distribution function of a combination utility and any of its gas or electric affiliates.[104]

OPC argues that "the additional complexities of the competitive market and the need to avoid market distortion in so many areas demands a common set of affiliate standards."[105] Staff submitted that "[A]ll regulated utilities . . . have the seeds of affiliate abuse within their organization if proper rules and structure are not required and enforced."[106] Staff concludes that there are not any unique characteristics which would exempt any of the types of regulated utilities. "All of the issues are, in general, the same for all types of utilities."[107]

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[100] Docket No. 60 at 28.
[101] *Id*.
[102] Docket No. 61 at 28.
[103] *Id*.
[104] *Id*. at 29.
[105] Docket No. 50 at 36.
[106] Docket No. 51 at 32.
[107] *Id*.

2. Commission Decision

The Commission concurs with the general consensus of the parties that, except for a separate GENCO code of conduct, gas, electric and combination utilities should be subject to the same rules and practices adopted in this case. In this way, no regulated entity will receive a competitive advantage, and inconsistencies can be avoided. However, the Commission has noted throughout this Order those instances in which a utility should be exempted from a particular requirement due to its size, its governing structure, or the nature of its particular service. To the extent GENCO rules are not specifically applicable to gas operations, a gas utility or division is not subject to those provisions.

. C. GENCO Codes of Conduct[108]

The relationship between electric generation companies ("GENCOs"), marketing affiliates, utilities and the provision of Standard Offer Service ("SOS") caused much debate both in this case and during the electric utility restructuring proceedings. The essence of the debate is the avoidance of favoritism by utilities and the development of a competitive and level playing field for electric generation. Robust competition is an essential ingredient of the restructuring process if consumers are to actually receive the benefits of competition, such as lower prices and additional choices and services. To a substantial degree, these issues are being addressed through GENCO Codes of Conduct. Therefore, the Commission will examine GENCO codes in detail.

[108] Issue No. 4: Should different standards of conduct apply to a regulated utility and its GENCO than to other regulated utilities and their unregulated affiliates? Issue No. 5: Should a utility's affiliate(s) be permitted to engage in the generation of electricity within the utility's distribution territory? Issue No. 12: What requirements should govern marketing of standard offer service for utilities and their affiliates?

1. Parties' Positions

During the restructuring proceedings, both BGE and APS filed GENCO Codes of Conduct as a part of that process. The Commission approved those GENCO codes when it approved their restructuring settlements. Pepco did not file a GENCO Code of Conduct because it is divesting all or practically all of its generating assets. Conectiv also did not submit a GENCO Code because it is divesting itself of substantial generating assets. Both the BGE and APS GENCO Codes of Conduct provide that they are effective until the Commission renders a decision regarding a GENCO Code of Conduct.

The BGE GENCO Code of Conduct has the following relevant provisions:[109]

- Until June 30, 2006, the BGE-GENCO must sell all of the generation output of the assets transferred under the Settlement (excluding all output sold to BGE for SOS) into the wholesale market.
- Until June 30, 2006 (the end of the BGE residential rate cap period) the BGE-GENCO shall be a separate subsidiary from BGE's retail marketing affiliate and separate from BGE.
- Until June 30, 2003, the BGE-GENCO shall not offer power or ancillary services at prices and terms more favorable to an affiliate for resale to retail electric customers in the BGE distribution service territory.
- While it serves as the SOS provider, BGE shall not be able to market or promote its SOS. However, this limitation shall not preclude BGE from providing unbiased information to customers that SOS is available and the terms thereof.

APS also filed a GENCO Code of Conduct as part of its restructuring proceeding.[110] The APS GENCO Code of Conduct stated that until January 1, 2004, any unregulated retail marketing affiliate of APS may sell or market to "retail electric customers" generation service in APS's Maryland distribution territory only through a subsidiary which is separate from the GENCO and APS. To the extent that an APS

[109] The BGE GENCO Code of Conduct is set out in full in its Settlement in Case Nos. 8794/8804.

marketing affiliate offers retail service in APS's Maryland territory, the GENCO shall offer power and ancillary services to non-affiliated licensed electric supplier up to the same amount and upon the same terms as the GENCO provides such services to APS's marketing affiliate. Information on GENCO sales to affiliates shall be simultaneously posted with the execution of any agreement for such sale on a publicly available electronic bulletin board. However, these provisions do not apply to sales by the GENCO to APS for SOS supply.

In addition, the APS-GENCO Code of Conduct provides that until January 1, 2004, to the extent that the GENCO makes sales to retail electric customers outside of the APS distribution territory, but within Maryland, the GENCO shall offer to sell to non-affiliated licensed electric suppliers at least 75 megawatts of power annually. (This is in addition to 180 megawatts of Warrior Run output being made available to the wholesale market under the APS Settlement). However, GENCO sales made using power purchased in the wholesale market or from facilities or assets built or acquired after the date of the APS Settlement,[111] or as part of a competitive bidding process, shall not be subject to these requirements. The APS Settlement Affiliate Code of Conduct provides that APS may not market SOS, but may provide unbiased information.

BGE stated that it views the GENCO standards contained in its settlement as an appropriate revision to the standards established by the Commission in Case No. 8747. Further, its settlement standards "represent a bargained-for exchange and address the legitimate concerns for the new retail sales market."[112] Because it is divesting its generation assets, Pepco has stated that "it should not be required to bear the costs of

[110] The APS GENCO Code of Conduct is Attachment 3 of its Settlement in Case No. 8797.
[111] The Settlement was signed by the parties effective September 23, 1999.
[112] Docket No. 79 at 8.

implementing a GENCO standard of conduct during its transition to a wires-only company."[113] Conectiv's settlement code of conduct provides that the "DPL-GENCO" shall be a separate corporate entity from "Delmarva" (now Conectiv). Conectiv noted that there are not any special requirements applicable to its GENCO affiliate in its settlement.[114] Conectiv is selling off some generation assets, so its share in the generation market is diminishing. Conectiv asserts that since it has no market power, nor ability to exercise market power in the generation market, it has no ability to "unfairly compete in that market."[115] According to Conectiv, "There is simply no factual basis for imposing a GENCO code on Conectiv to govern the transactions between the GENCO and the retail marketing affiliate."[116] Neither the gas utilities nor Choptank address this issue in detail because they do not presently have any generation assets.

In addition to BGE, many other parties support BGE's Genco Code of Conduct. Enron/Statoil urges the Commission to adopt BGE's settlement standards as the generic GENCO standards, revised to apply such standards to all electric companies and to amend the standards to apply to the longer of a utility's stranded cost recovery period or the term of its SOS obligation.[117] Enron/Statoil argued that the "purpose of the GENCO code is to minimize the opportunity for unduly discriminating behavior between the utility… and new GENCO affiliate and any retail marketing affiliate of the utility."[118] The Joint Commenters say that Enron/Statoil "propose appropriate rules to address these circumstances."[119] The Alliance also supports "standards of conduct for GENCOs that

[113] Docket No. 83 at 12.
[114] Docket No. 97 at 5. Conectiv's Settlement is found in Case No. 8795.
[115] *Id*. at 3.
[116] *Id*.
[117] Docket No. 85 at 15-16.
[118] Docket No.104 at 5-6.
[119] Docket No. 84 at 19.

are different from those applied to the relationships of utilities and other affiliates."[120] Enron/Statoil concludes that "a GENCO code is the single most essential change to the Case No. 8747 standards."[121]

MAPSA emphasized the need for standards of conduct related to utility affiliated generation companies. MAPSA noted that problems related to utility market power and competitive market development are well documented in Pennsylvania. Also, market inertia is a given. Consequently, "MAPSA strongly recommends that the Commission establish, at a minimum, the BGE standards as the foundation for developing more comprehensive standards for all state utilities that operate or will transfer title to utility generation assets to an affiliate."[122] "These comprehensive standards should include an expeditious decision-making process and stiff penalties to the utility for infractions on the part of the utility or the affiliate."[123]

Two GENCO-related issues received particular discussion, affiliate electric generation marketing practices and the marketing of SOS. The utilities take the position that an affiliate should be permitted to sell generation supply within the utility's service territory. Since the Act permits utilities to procure electricity for SOS from an affiliate, Conectiv stated that "[I]t would, therefore, be inconsistent with the . . . Act to preclude an affiliate from engaging in generation of electricity within the utility's distribution service territory."[124] "So long as appropriate standards of conduct are in place . . .to govern the transactions and relationships between the utility and its core-service affiliates, there is no need to handicap utility affiliates in their efforts to compete in any marketplace."[125]

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[120] Docket No. 59 at 9.
[121] Docket No. 104 at 7.
[122] Docket No. 63 at 8.
[123] *Id*.
[124] Docket No. 53 at 16.
[125] *Id*. at 16-17.

Pepco stated that "economic theory and evidence from other deregulated electricity markets indicate that generation markets are intensely competitive."[126] Pepco concludes that "there is no reason to deprive consumers of an opportunity to buy power from their distribution utility's power producing affiliate."[127] WGL noted that "[I]f an affiliate attempted to purchase or build facilities to generate electricity within the utility's distribution territory, then there are state requirements already in place that provide the PSC the opportunity to review the proceedings to ensure that there are no unfair advantages to the utility distribution company."[128]

As for Standard Offer Service, the BGE-GENCO Code of Conduct and the APS Affiliate Code of Conduct adopted as part of their respective settlements prohibit the marketing of SOS, although unbiased information may be provided to consumers. Pepco has stated that it "will not promote standard offer service."[129] WGL asserted that "incumbent utilities should not promote standard offer service as a 'competing' service."[130] Only Conectiv and Choptank took a contrary position. Conectiv argues that utilities "should be able to market, advertise or otherwise provide information regarding" SOS, provided that the information is factual and that the utility does not imply that SOS is more reliable than service from competitive suppliers.[131] Choptank stated that it "agrees wholeheartedly with Conectiv" that utilities should be able to market SOS.[132] "We believe this is particularly true for a member-owned Cooperative."[133] Choptank asserts that SOS is an important service and consumers should be aware of it.[134]

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126 Docket No. 64, Appendix A at 2.
127 *Id*.
128 Docket No. 55, Appendix A at 2.
129 Docket No. 64, Attachment A at 4.
130 Docket No. 55, Appendix A at 5.
131 Docket No. 53 at 27.
132 Docket No. 70 at 8.
133 *Id*.
134 *Id*. at 9.

The marketers generally oppose permitting a GENCO to market electricity. Enron/Statoil takes the position that a utility's GENCO should not be permitted to sell power at retail within the utility's distribution territory while the utility is recovering stranded costs or while the utility is providing SOS, whichever is longer. Enron/Statoil's position is based upon their belief that GENCOs receive advantages from below-market transfers of assets from the utility to the GENCO, that there is inherent potential for self-dealing, and that the need exists for GENCOs to sell their output into the wholesale market. Retail sales by affiliates would not be inappropriate after the stranded cost or SOS period, in the absence of market power.[135]

The Joint Commenters say that the Commission "should not permit a utility's affiliate(s) to engage in the generation of electricity within the utility's distribution territory unless and until the utility has voluntarily divested all of its generation assets via a competitive bid process."[136] This will prevent a utility from leveraging its incumbency advantages to the detriment of consumers, according to the Joint Commenters.

The marketers also oppose the promotion of SOS because, they say, it would be anti-competitive. The Alliance argued that SOS is a "safety net service."[137] Further, "SOS should not be marketed as a competitive alternative for customers by the utilities or by affiliates on the utilities' behalf."[138] According to the Alliance, "the terms and conditions of SOS are most appropriately distributed via the State's Consumer Education Campaign."[139] The Alliance concludes that "[m]arketing of the SOS would create an insurmountable barrier to competitors and must be strictly prohibited."[140] The Joint

[135] Docket No. 60 at 21.
[136] Docket No. 61 at 10.
[137] Docket No. 59 at 16.
[138] *Id*. at 17.
[139] *Id*.
[140] *Id*. at 18.

Commenters say that the Commission should prohibit the promotion of SOS and require GENCOs to be separate subsidiaries from retail marketing or the SOS function. The Joint Commenters continue to advocate a single uniform code of conduct for all Maryland energy utilities. Lastly, they say that the Commission "should also consider extending the Standard Offer concept to the utilities' natural gas supply operations."[141]

OPC argued that since "generation ownership is allowed in the local area, clear separation must be required between generation, retail marketing, and default service."[142] This means the GENCO affiliate must be separate from both the utility and any retail affiliates. Since bilateral transactions between the GENCO and the SOS provider are permitted, OPC submitted that the Commission "must be ready to regulate such bilateral transactions to assure that they are made on an arm's length basis" once the rate cap period ends.[143] OPC also stated that SOS "should not be actively promoted by the utility in the initial three year period or if the utility is awarded the right to continue to offer standard offer service after the end of the three year period."[144] According to OPC, "This restriction is necessary to encourage the development of a competitive market without the utility attempting to hold on to customers."[145]

Staff has proposed four separate standards for affiliates, one of which is a GENCO standard. "Staff recommends that during the transition period, the generic standards based on the individual settlement agreements for GENCOs should apply."[146] Staff also noted that bilateral contracts between Maryland GENCOs and utilities "could be a source of concern."[147] If Staff's recommendations for GENCOs are adopted (full

[141] Docket No. 61 at 22.
[142] Docket No. 50 at 15.
[143] *Id*. at 16.
[144] *Id*. at 29.
[145] *Id*.
[146] Docket No. 51 at 15.
[147] *Id*. at 17.

structural separation with standards of conduct appropriate for marketing affiliates), electric company consumer protection and any adverse competitive effects would be accounted for in an adequate manner.[148] Staff noted that "[A]ll non-utility parties agree that the utility should not engage in promotion of SOS or in any way acknowledge it as a 'competitive service'".[149] Staff supports its generic version of the settlement standards on this issue.[150]

2. Commission Decision

The Commission finds that it is appropriate to adopt a GENCO Code of Conduct because it will foster competitive electric generation markets, minimize market power, and help to eliminate any inherent advantages that a GENCO might currently possess. The Commission concurs with the prevailing sentiment of the parties that the BGE settlement GENCO standard should be adopted as the generic GENCO standard. It should also be noted that in adopting this generic GENCO standard it will be made applicable to any utility operating in Maryland that does business with any company affiliate that acquires electric generating assets in the future. In this way, another utility that has an affiliate or acquires generation assets will be subject to the same standards as the current electric utilities.

The Commission is not unmindful of the extensive negotiations that led to the APS GENCO code of conduct. No party to the APS stranded costs proceeding, Case No. 8797, opposed that settlement. In particular, Staff and OPC supported that settlement and the Commission recently approved it. Therefore, during the term of the residential price cap in Case No. 8797, APS shall conduct its activities consistent with its GENCO code of conduct rather than the generic code adopted herein. However, the Commission will

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[148] *Id*. at 16.
[149] Docket No. 73 at 13.

continue to monitor the effects of this decision on the development of a competitive market and reserves its right to institute a proceeding to review the APS GENCO Code of Conduct, if necessary.

As for Pepco, the Commission will grant its request to be exempt from the GENCO code of conduct adopted herein because Pepco will have no generating assets, or be retaining only insignificant generating assets. However, if a Pepco affiliate acquires new generation assets, then the GENCO code of conduct will apply. On the other hand, Conectiv will be subject to the generic GENCO code of conduct adopted herein. As Conectiv noted in its comments, there are not any special requirements applicable to its GENCO affiliate in its settlement, Case No. 8795. Unlike Pepco, Conectiv will retain sufficient generation assets to warrant the application of the generic GENCO Code of Conduct. Moreover, as the end of the transition periods approach, the Commission will determine the appropriateness of extending or modifying the provisions of the GENCO Codes of Conduct in light of the status of generation and retail electricity markets at that time.

In this proceeding, the Commission has adopted a generic GENCO Code of Conduct that requires a GENCO to be a separate subsidiary from the retail marketing affiliate and separate from the utility until June 30, 2006. Therefore, a GENCO may not itself "market" the electricity produced from its generation assets. The APS GENCO Code of Conduct has a similar provision applicable only to the APS distribution territory.

Except for SOS, the GENCO will be required to sell all generation output into the wholesale market. (APS has different terms that have a similarly non-discriminatory impact). Consequently, the marketing affiliates will be required to procure electric

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[150] *Id*.

supply in the wholesale market for subsequent sale to retail customers. Inasmuch as retail marketing affiliates will have to procure electricity in the wholesale marketplace, they will not possess any market power. Therefore, it is appropriate to encourage retail marketing affiliates to participate in the competitive retail market in the utility's existing service territory. In fact, the Commission notes that both the BGE and APS stranded cost settlements exhibit an effort by the settling parties to require the utility's retail marketing affiliate to participate in the local market, on a non-discriminatory basis.

In conclusion, until June 30, 2006 a GENCO (except as provided in the AP's GENCO code of conduct) must sell all of its output not dedicated for SOS, into the wholesale market. Retail marketing affiliates may, and in fact are encouraged, to participate in the local retail market, on a non-discriminatory basis as explained herein.

There is almost unanimous agreement among the parties that a utility should not be permitted to market standard offer service. To begin with, SOS is not a competitive service; it is a default service. In addition, the Commission desires to eliminate unnecessary barriers to competition. Overcoming customer inertia may itself be difficult and this should not be compounded by the promotion of a service that is not intended to be a competitive service. As the Alliance noted, SOS is a "safety net service." No party presented any persuasive evidence to convince the Commission that there is a public benefit to marketing SOS. Therefore, consistent with the near unanimous position of the parties, the Commission will prohibit the marketing of SOS by utilities. A utility may, however, provide unbiased educational information to customers that SOS is available and the terms of SOS. The Commission will address this issue again if, and when, an entity other than the electric utility is considered as the provider of SOS.

D. Transfer of Assets[151]

1. Definition

(a) Parties' Positions

In Case No. 8747, the Commission determined that "utility assets are tangible property included in a utility's rate base."[152] The utilities agree with this determination. Pepco asserted that there is "no reason to alter this definition."[153]

The marketers take a differing view. The Alliance argued that the Commission's definition of a utility asset "fails to recognize the value of services and personnel that are also integral parts of the utility and which can be used to substantially benefit the utilities' affiliates."[154] Further, if the Commission is not willing to classify utility personnel as "assets" and require appropriate valuation of, and compensation for their services, then the Commission "must ensure that no transferring of personnel is permitted."[155] The Alliance concludes that utilities should not serve as the training ground for affiliate employees.

The Joint Commenters state that a "utility asset" should be defined "as all utility-owned or controlled property, real or intangible, that would be saleable in a market."[156] They argue that the Commission's definition "is too narrow because it leaves numerous opportunities for the utility or its affiliates to exploit the utility's incumbency advantages in unfair and anti-competitive ways."[157] The Joint Commenters state that the definition of "utility asset" "does not hinge on who owns the asset."[158] Rather, the question is

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[151] Issue No. 7: What value should be used when utility assets or affiliated assets are sold or transferred between the companies (book or fair market value)?Issue No. 8: What constitutes a utility asset?
[152] Case No. 8747 at 50.
[153] Docket No. 64, Attachment A at 3.
[154] Docket No. 59 at 11.
[155] *Id*.
[156] Docket No. 61 at 12.
[157] *Id*.
[158] *Id*.

whether the value of the asset is a result of the utility's provision of franchise monopoly services."[159] In that case, affiliates will gain an unfair advantage if they have access to these assets on terms and conditions that are more favorable than those available to competitors. The Joint Commenters emphasize, as an example, that the brand name and reputation convey an unfair advantage and that the utility should be required to charge its affiliates a royalty for use of the utility's brand name and logo.

OPC submitted that utility assets "include not only physical assets but intellectual property created by the utility, any proprietary information, computer data bases owned by the utility, and access to utility services such as billing envelope" and which exist solely because of the existence of the regulated utility and because of billing functions paid for entirely by ratepayers.[160] Intellectual property includes the utility logo and other proprietary materials. OPC concludes that transfers of these intangible assets, that can be used by more than one entity, should be prohibited unless they are available to others at the same cost.

The Maryland Energy Administration ("MEA") asserts that the Commission's definition of assets "is unjustifiably too narrow."[161] It asserted that non-tangible assets can be associated with income and are routinely included on utility balance sheets and may or may not qualify for inclusion in rate base.[162] "Because non-tangible assets as well as tangible assets can be the source of gain when transferred to an affiliate, the MEA believes the Commission should discard the recognition of only tangible assets

[159] *Id*.
[160] *Id*.
[161] Docket No. 72 at 2.
[162] *Id*.

incorporated in its Case No. 8747, Order No. 74038 affiliated transactions standards and take a commensurately broader view of utility assets."[163]

Staff takes the position that utility assets "should be construed as those economic resources that have historically either been included in rate base or necessarily represent cost components devoted to utility operations that would be typically reflected in rate base."[164] Staff does not include intangible assets in its definition because "historically these assets have not been included in the cost of service."[165]

(b) Commission Decision

Many of the parties asserted that the Commission's definition of utility assets adopted in Case No. 8747 is too narrow. The Commission agrees. The Commission finds that the definition of a utility asset should encompass intangible property as well as tangible property. Clearly intellectual property, computer data, access to the billing envelope and any other proprietary information has substantial value.[166] These valuable assets are the product, at least in part, of the utility's provision of State-franchised monopoly services, ratepayer funded support, and State regulation and protection. Consequently, the Commission believes that it is appropriate to require that intangible assets be subject to the same principles and allocation procedures as tangible assets.[167]

2. Valuation

(a) Parties' Positions

In Case No. 8747, the Commission found that "asymmetric pricing should govern the sale or transfer of assets between a utility and its affiliates."[168] Asymmetric pricing

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163 *Id*. at 2-3.
164 Docket No. 51 at 18.
165 Docket No. 73 at 10.
166 As discussed in detail in Subsection H, utility names and logos have significant value.
167 Although some parties discussed employees within the context of defining assets, the Commission addresses issues relating to employees within the context of the sharing of services, in Subsection E.
168 Case No. 8747, Order No. 74038, 89 MD PSC 54, 79 (1998).

requires that transfers of assets from the regulated utility to an affiliate should be recorded at the greater of book cost or market value while transfers of assets from the affiliate to the regulated utility should be at the lesser of book cost or market value. This principle had been previously adopted in Case No. 8577 and was affirmed in Case No. 8709.

The utilities oppose asymmetric pricing. Dr. Gordon stated that "the affiliate should pay no less than the utility's appropriately specified incremental cost of providing an asset or service."[169] "The use of fully-allocated cost by utilities . . . more than meets this criterion, and builds in a 'margin of protection' that provides a high level of assurance that ratepayers are not subsidizing the firm's competitive ventures."[170] According to Dr. Gordon, "payments by affiliates that are above incremental costs represent overcompensation to ratepayers, limits the benefits of competition in other markets and punishes companies for being affiliated with utilities."[171]

Conectiv argues that "rather than apply asymmetrical pricing across the board to all utilities, it is appropriate for utility companies to provide cost allocation manuals to the Commission . . . to ensure that . . . ratepayers do not subsidize competitive activities."[172] Further, a waiver process should be established for accounting standards. During the period of capped rates, "concerns about affiliate transactions should be virtually irrelevant since it is [the utility] . . . and its shareholders that are at risk irrespective of the price at which the transaction occurs."[173]

[169] Docket No. 56 at 19.
[170] *Id*.
[171] *Id*.
[172] Docket No. 53 at 19.
[173] *Id*. at 19-20.

Pepco submitted that "[C]ustomers will benefit if utilities are permitted to use fair market value pricing, instead of fully allocated costs, in appropriate circumstances."[174] WGL asserted that assets should be transferred at fair market value because this "is consistent with the widely accepted practice of employing competitive procurement policies whenever possible."[175] Chesapeake concurs.[176] Columbia argued that asymmetric pricing constitutes "over protection" for regulated utility customers and should be abandoned.[177] NUI stated that "requiring the transfer price to be set at net book value or prevailing market price regardless of the transaction's direction" will protect ratepayers and encourage economic efficiency.[178] When a prevailing market price cannot be established, NUI recommends a negotiated price no lower than book value, or possibly an appraisal.[179]

The marketers support the continuation of asymmetric pricing. The Joint Commenters say that the "asymmetric pricing principle continues to provide valuable protections for monopoly distribution ratepayers, as well as competitors."[180] "To aid in applying the principle, the utility should bear the burden of establishing the market value of goods and services exchanged between itself and its affiliates."[181] Enron/Statoil supports asymmetric pricing because it will "prohibit cross-subsidization by the utility's ratepayers of unregulated activities and eliminate the potential for anti-competitive pricing that favors utility affiliates.[182] The Alliance stresses that the Commission must

[174] Docket No. 64 at 7.
[175] Docket No. 55, Attachment A, p. 3.
[176] Docket No. 54, Comment on Issues 7 & 8.
[177] Docket No. 49 at 4.
[178] Docket No. 69 at 6.
[179] *Id*.
[180] Docket No. 61 at 12.
[181] *Id*.
[182] Docket No. 60 at 22.

ensure that no confusion results for customers from asset transfers, such as trucks from BGE to BGE Home.[183]

OPC also supports asymmetric pricing. However, OPC suggested that for physical assets with a net book value of $100,000 or less, the asset could be transferred at net book value to streamline the process. OPC suggests that the Commission maintain access to data regarding inter-affiliate transfers to guard against abusive practices.[184]

Staff also supports the continuation of asymmetric pricing of assets. The purpose for this policy "is to guarantee that the regulated utility operations are made whole for assets that are transferred to an affiliate and to ensure that assets are not transferred into the utility at inflated prices."[185] "Staff believes this methodology provides appropriate security to prevent any self-dealing that may occur."[186] Staff suggests that assets with a book value below $5,000 may be transferred at book value for administrative efficiency.[187] Assets with a book value greater than $100,000 should require an independent assessment of the value of the transferred assets at the time of transfer.[188]

(b) Commission Decision

The Commission has endorsed the principle of asymmetric pricing on three previous occasions. As the Commission stated in Case No. 8577, "[t]he purpose of this principle is to guarantee that . . .[the utility] is made whole for any assets it transfers away from regulated operations, and to ensure that assets are not transferred to regulated operations at inflated prices."[189] The Commission also determined that asymmetric pricing "is fair to utility ratepayers, provides a reasonable insurance policy against

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[183] Docket No. 59 at 9-10.
[184] Docket No. 50 at 18.
[185] Docket No. 51 at 17.
[186] Docket No. 73 at 9.
[187] *Id*.
[188] *Id*.
[189] Case No. 8577, Order No. 72107, 86 Md PSC 225, 234 (1995).

improper self-dealing, and constitutes a necessary protection against the possible improprieties that can result from a corporate structure that does not completely separate regulated from unregulated operations."[190] The only parties to this proceeding that have opposed asymmetric pricing are the utilities. The utilities have not advanced any new arguments to persuade the Commission to alter its current policy. Therefore, it is appropriate to continue the principle of asymmetric pricing of assets.[191]

E. Shared Services and Employees/Loans and Guarantees[192]

1. Services and Employees

(a) Parties' Positions

The utilities generally support permitting employees and services to be shared because of economies of scope and scale. Dr. Gordon asserted that limitations on sharing employees should be "carefully considered, narrowly drawn, and based on legitimate concerns for consumer welfare."[193] However, he also stated that it is inappropriate to share employees "who possess non-public, market sensitive information."[194] BGE noted that it "supports the Commission's rules and procedures governing the sharing of employees and/or services as established in Case Nos. 8577, 8709, and 8747 as applied in BGE's Cost Allocation Manual on file with the Commission."[195]

Conectiv noted that in Case No. 8747, the Commission determined that "a utility must identify and separate its affiliates' operational and managerial employees from those of the utility in order to avoid cross-subsidization and to assure fairness in the

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[190] *Id*.
[191] Any transfer of a utility name or logo is specifically subject to the Commission's findings and decision as stated in Subsection H.
[192] Issue No. 9: What specific rules and procedures should the Commission adopt governing the sharing of employees and/or services between the utility and its affiliate?
[193] Docket No. 56 at 20.
[194] *Id*.
[195] Docket No. 57 at 6.

competitive marketplace."[196] "[F]or those employees and services which can be shared, a utility must identify them and seek Commission approval for such sharing."[197] Conectiv requests that the Commission clarify that the operational and managerial separation requirements be applied only to a retail electric or gas marketing affiliate that provides the same product as the utility in Maryland.[198] Conectiv asserted that while core service affiliate Standard No. 5 requires physical separation of core affiliates, there is no corresponding requirement for non-core affiliates.[199] Conectiv concludes that consistent with this approach, Case 8747 should be "clarified to confirm that it is not applicable to non-core-service affiliates."[200] Conectiv also stated that it "agrees that the Commission should ensure that costs are properly accounted for and allocated for any facilities or employees shared" with affiliates.[201] This is the purpose of Conectiv's Cost Allocation Manual.[202] Conectiv concludes that applying these separation requirements to all affiliates "would impair beneficial competition."[203] Dr. Gordon supports Conectiv's position.[204] Pepco also supports Conectiv. Pepco asserted that "there is no economic or ratepayer protection rationale for applying . . . [core standard No. 5] to 'non-core' service affiliates."[205]

Choptank also asserts that the Commission needs to address confusion surrounding this issue.[206] Choptank argued that the Commission needs to clarify that

[196] Case No. 8747 at 45.
[197] *Id*.
[198] Docket No. 53 at 21.
[199] Case No. 8747, Core Service Affiliate Standard No. 5 stated: "A utility and its core-service affiliate(s) shall operate from physically separate locations to avoid the inadvertent sharing of information."
[200] Docket No. 53 at 22.
[201] *Id*. at 23.
[202] Conectiv has a Cost Allocation Manual that has been filed in Delaware. A copy has been provided to this Commission. However, this Commission does not currently require Conectiv to file a CAM.
[203] Docket No. 53 at 22.
[204] Docket No. 56 at 20.
[205] Docket No. 64, Attachment A at 3.
[206] Docket No. 70 at 6.

identification and separation of operational and managerial employees of a utility and its affiliates should only apply to affiliates engaged in an unregulated business which was formerly a monopoly offering.[207] Choptank argues that placing restrictions on managers or employees used by non-core affiliates, or even requiring approval prior to any sharing is beyond the Commission's authority.[208] "Choptank thinks it should be sufficient to inform the Commission of such activities instead of asking for permission."[209] Choptank argues that Maryland utilities and affiliates should not be barred from using personnel to any greater extent than competitors.[210] "Choptank believes that it is vital to the interests of its members and for the State that the State's Utilities are not put at a disadvantage when trying to compete for non-core business."[211]

WGL asserted that "[R]ules and procedures for the sharing of employees should be based on the type of services being provided by the employees. A distinction can be drawn between 'operational' and 'non-operational' employees."[212] According to WGL, non-operational employees should be permitted to provide services to affiliates because it benefits ratepayers. "The allocation of the costs of these services to the affiliate reduces costs to ratepayers."[213]

Chesapeake supported the standards adopted in Case No. 8747. It argued that those cost accounting principles and standards of conduct "are the appropriate mechanisms to govern the sharing of employees and/or services between the utility and its affiliates and will ensure that the affiliate is not being subsidized by the utility

[207] *Id*.
[208] *Id*.
[209] *Id*. at 7.
[210] *Id*.
[211] *Id*. at 6-7.
[212] Docket No. 55, Appendix A at 4.
[213] *Id*.

ratepayers."[214] Chesapeake also supports Conectiv's position that rules for sharing employees and services should only apply to interactions with core-service affiliates.[215]

NUI insisted that the utility should be permitted to share employees and services with affiliates "for all functions which would not cause the utility to have an unfair competitive advantage due to the utility's provision of monopoly service."[216] According to NUI, services that could be shared include: "accounting, human resources, legal, treasury, information systems (with appropriate safeguards), executive, and any other service that would not create an unfair advantage to a competitor in the market."[217] NUI opposed full structural separation and argued that there is "no rationale as to why such extreme measures are necessary."[218] NUI emphasizes that it is particularly important for smaller utilities to generate significant economies of joint use with affiliates.

The marketers take a much more stringent view of sharing employees and services. The Mid-Atlantic Propane Gas Association ("PGA") indicated that the utility and affiliate should maintain separate work forces. "At no time . . . [should] any personnel be employed simultaneously for both the regulated utility or electric cooperative and its affiliates(s)."[219] Enron/Statoil insisted that there should be "absolutely no sharing of employees and/or services between the utility, any GENCO, and any marketing affiliate of the utility, with the possible exception of certain 'corporate support' type functions."[220] Further, "to the extent some might consider, as a 'service',

[214] Docket No. 54
[215] *Id*.
[216] Docket No. 69 at 7.
[217] *Id*.
[218] *Id*. at 8.
[219] Docket No. 45 at 2.
[220] Docket No. 60 at 22.

the offering of loans or loan guarantees by a utility to, or on behalf of, any utility affiliate, it should be clear that this kind of service is prohibited."[221]

The Joint Commenters recommend a detailed list of rules for sharing employees and services between utilities and affiliates.[222] "As a general principle, such joint utilization shall not allow or provide a means for the transfer of confidential information from the utility to the affiliate, create the opportunity for preferential treatment or unfair competitive advantage, lead to consumer confusion, or create significant opportunities for cross-subsidization of affiliates."[223] Except for certain corporate support functions, utilities and affiliates should not be permitted to jointly employ the same employees, or make temporary or intermittent assignments or rotations, according to the Joint Commenters. A utility should also be required to track and annually report publicly all employee movement between the utility and affiliates. The Joint Commenters say that their proposed rules "represent a tradeoff between the protection of competition through strict structural separation and the preservation of some scope economies through shared corporate support functions."[224]

The Joint Commenters make a point that a utility should not be permitted to guarantee the debt of an affiliate. There are at least two reasons for the Commission to reconsider its previous position:

> First, the Commission's reduced reliance on traditional cost-of-service regulation makes it more difficult to use periodic cost-of-capital reviews to protect monopoly ratepayers against the possible harmful effects of such debt guarantees. Second, the potential magnitude of the general-related debt that the distribution utility might be asked to guarantee is much greater in relation to the remaining

[221] *Id*.
[222] Docket No. 61, p. 15-19.
[223] *Id*. at 16-17.
[224] *Id*. at 18.

> utility assets than any previously contemplated affiliate debt to be guaranteed.[225]

The Joint Commenters conclude that these risks "outweigh any possible gain to Maryland consumers that would result from giving utility affiliates access to lower cost debt."[226] Finally, the Joint Commenters say that "the public policy benefits of protecting competition through strict structural separation generally outweigh the scope economies achievable through sharing of employees and services."[227]

The Alliance recommends that all sharing and transferring of personnel be prohibited. "The Alliance's experience indicates that the utilities are generally incapable of adhering to Commission orders respecting employee sharing, and are similarly incapable of properly accounting for and properly charging employee time above or below the line."[228] According to MAPSA, "[I]nappropriate relationships between utilities and retail affiliates drive competitors out of the marketplace."[229]

OPC also offered extensive recommendations on this issue. OPC stated that the "greater the possible degree of separation, the better."[230] In addition, "shared services should be limited to corporate governance and similar services."[231] OPC supports a requirement that each utility submit a CAM for approval. By requiring approval of the manual in advance, OPC noted that the Commission could avoid surprise changes in allocation methods between rate cases. OPC emphasizes that it is important that separation be maintained for affiliates operating in the utility's service area and for energy supply and trading affiliates. OPC urged that shared employees "should be

[225] *Id*. at 19.
[226] *Id*.
[227] *Id*. at 18.
[228] Docket No. 59 at 11-12.
[229] Docket No. 63 at 10.
[230] Docket No. 50 at 20.
[231] *Id*.

compensated on an asymmetric basis (the higher of cost versus value)."[232] Generally, OPC recommends that transfers of employees to affiliates should require the affiliate to pay 25% of a year's salary to the utility "to reflect the value to the affiliate of using the utility as a personnel agency."[233] In addition, such employees should be prohibited from returning to the utility for two years "to prevent frequent exchange of employees and the information they bring with them."[234] Other goods and services, OPC argued, should be compensated at the higher of market value or cost, or cost plus a 10% royalty. Goods or services purchased by the utility in excess of $50,000 should require a competitive bidding process. OPC suggested that any premiums or royalty payments "must be placed in an account for refund to customers on an annual basis."[235]

OPC also addressed the issue of loans and loan guarantees.[236] Case No. 8747 required that loans from a utility reflect a market rate of interest. According to OPC, market rate should reflect the credit standing of the affiliate on "a stand-alone basis."[237] Moreover, OPC noted that: "[A]ny rate which is less than 25 basis points above the market rate appropriate for the term of the loan and the credit rating of the utility should be deemed unreasonable in the absence of clear evidence that the affiliate standing alone has the same credit rating as the utility."[238] OPC also recommends imposing an annual fee of 25 basis points to the amount guaranteed to compensate ratepayers for the value of the guarantee.

[232] *Id*. at 21.
[233] *Id*.
[234] *Id*.
[235] *Id*. at 22.
[236] *Id*.
[237] *Id*.
[238] *Id*.

Staff argued that goods and services that are transferred "should be based on a fully-distributed cost."[239] This is based upon the "concept of flowing all costs to relevant business activities . . . so that reasonable cost attribution occurs."[240] Staff supports a continuation of the policy in 8747 of separating operational and managerial employees "in order to avoid concerns of cross-subsidization and to assure fairness."[241] The utility should seek approval to share employees and services and provide certain information to the Commission. In addition, Staff recommends implementing a competitive bidding process for utility purchases from affiliates with an estimated purchase price of $50,000 or more. Staff supports the sharing of non-operational resources. Finally, for services that can be marketed by the utility, "it must be priced at market value rather than fully-distributed cost and it should be made available to the market on the same terms and conditions as those offered to the affiliate."[242]

(b) Commission Decision

The Commission herein reaffirms in principle the findings adopted in Case No. 8747, and certain previous proceedings, that some degree of sharing of utility employees and services is appropriate. The Commission again rejects the concept of strict structural separation. Furthermore, sharing of certain general corporate services employees produces opportunities for greater efficiencies that can reduce the cost of service for ratepayers while avoiding adverse impacts on the competitive market. If these costs are properly allocated, this results in a net benefit for ratepayers. As we stated in Case No. 8747:

[239] Docket No. 51 at 18.
[240] *Id*.
[241] *Id*.
[242] *Id*. at 19.

> Although customers do not acquire a proprietary interest in a utility's assets through the payment of rates for service, they are, nevertheless, responsible for the total cost of service. If any portion of this total cost can be allocated to an affiliate which is using assets included in that cost of service, ratepayers are entitled to an offset . . . Accordingly, we find that a fully distributed cost methodology should be used in allocating joint costs between a utility and its affiliates.[243]

However, as previously noted, there must be limits because of the potential adverse consequences of customer confusion, ratepayer cross-subsidization, transfer of confidential utility or customer information or preferential treatment in the provision of utility service. Specifically, the Commission finds that utility operational and managerial employees may not be shared between a utility and a non-core affiliate, just as they are prohibited from being shared with core affiliates.

Generally, employees providing corporate support-type services may be shared. However, market research, public relations, and advertising employees, as well as major account executives and other marketing staff employees, customer service representatives, and accounts receivable staff may not be shared.

As a general matter, the Commission finds accountants and lawyers may not be shared between a utility and an affiliate. Legal services and accounting personnel may be shared only under limited circumstances. For instance, accounting personnel may be shared for the purpose of establishing corporate accounting policies and standards, producing consolidated corporate financial and tax statements, and for preparing consolidated financial records or reports. Legal personnel may not share responsibilities for contract negotiations and regulatory affairs with an affiliate but may share responsibilities for consolidated corporate support, such as OSHA and ERISA

[243] Case No. 8747, Order No. 74038, 89 MD PSC 54, 70 (1998).

compliance, or preparation of certain Internal Revenue Service or Securities and Exchange Commission filings.

While the broad parameters of the Commission's policy on the sharing of employees is set forth herein, the Commission intends to review each utility's proposed employee sharing plan to ensure its compliance with these policies. Prior to any sharing, the utility must identify the employees and their functions that it seeks to share with either a core or non-core affiliate and obtain prior Commission approval. To the extent that employees are being currently shared, they must be identified immediately for the Commission and a prompt request for approval must be filed. To the extent the utility shares any employee with an affiliate that is contrary to the policies adopted herein, such sharing must cease as soon as practicable.

The Commission hereby reaffirms previous decisions that all joint costs for services, including shared employees, will be allocated between the utility and its affiliates upon the basis of a fully distributed cost methodology. However, when services can reasonably be marketed by a utility to the public, the fair market value of such services must be allocated as the imputed costs to the subsidiary. Appropriate costs will be allocated with the sharing of services and the utility will receive a commensurate return for the sharing of services and employees. This will benefit ratepayers by reducing the cost of service. The Commission declines to extend asymmetrical pricing principles to services and employees and rejects OPC's suggestion that an additional fee of 10% to 25% should be added to the cost of utility services in certain instances.

2. Loans/Guarantees

(a) Decision in Case No. 8747

The Commission specifically addressed the issues of affiliate borrowing and utility loan guarantees in Case No. 8747. In that proceeding the utilities, not surprisingly, argued that they should be permitted to make loans to affiliates and issue guarantees on their behalf. They asserted that as long as there was no ratepayer subsidization, competition should not be impeded.[244] Further, they said that standard regulatory practices could be used to prevent any adverse impact on ratepayers.[245] The utilities emphasized that they should be permitted to guarantee loans to affiliates without any fee being imposed or imputed for this service because affiliate loan guarantees are a standard business practice.[246] However, at least one utility stated that utilities in a holding company structure are not allowed by PUHCA to guarantee loans (although a non-utility parent may do so).[247] Finally, some utilities argued that pursuant to the PSC Law, the Commission may only regulate loan guarantees made by utilities organized under Maryland law.[248]

Equally not surprising, the marketers opposed these types of activities. They emphasized that affiliates should stand alone and not be subsidized by ratepayers.[249] Marketers argued that loan guarantees place the utility's credit worthiness at risk, which might eventually be reflected in rates for service.[250] The marketers also complained that utilities can raise capital at costs below that of most small businesses and therefore, loan

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[244] Case No. 8747, Order No. 74038, 89 MD PSC 54, 83 (1998).
[245] *Id*.
[246] *Id*. at 80.
[247] *Id*. at 80 and 92.
[248] *Id*. at 80; see §§5-202, 5-203 and 6-101 (formerly §24(b)(4)).
[249] *Id*. at 80.
[250] *Id*.

guarantees are a non-competitive subsidy to affiliates.[251] The marketers also stated that all borrowings by affiliates must be at market rates.[252]

OPC emphasized in Case No. 8747 the need for certain restrictions on loan guarantees. These would be designed to avoid placing the utility's credit standing at risk and ensure that ratepayers are not harmed.[253] Staff concurred with a previous Commission position that utilities should be permitted to guarantee the debt of an affiliate, provided that the fair market value of the guarantee is imputed to the regulated activities of the utility.[254] However, Staff took the position that utilities should not be permitted to loan affiliates' money because the utility is not a financial institution.[255] OPC agreed that long-term borrowings should not be allowed.[256]

In Case No. 8747, the Commission determined that upon its review and approval, utilities would be allowed to lend money to their affiliates at rates the affiliate could obtain in the open market.[257] The Commission found that this would avoid certain transactions' costs without harming ratepayers.[258] The Commission also determined that "under the appropriate circumstances" it would approve loan guarantees.[259] The Commission determined that authority to permit such requests is found in the PSC Law.[260] The Commission also determined that an additional fee for such guarantees would not be required because non-Maryland corporations make loans to affiliates without a fee being imposed.[261]

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[251] *Id*.
[252] *Id*. at 83.
[253] *Id*. at 80.
[254] *Id*. See Case No. 8710.
[255] *Id*. at 83.
[256] *Id*.
[257] *Id*.
[258] *Id*. at 83-84.
[259] *Id*. at 81.
[260] *Id*., See § 5-202, § 5-303, § 6-101, § 6-102 and § 6-103.
[261] *Id*. at 81.

Loans and guarantees present another issue that should be reexamined in light of changing circumstances in the restructuring energy marketplace and the record herein. With electric generation assets being transferred to GENCOs and a myriad of new affiliate relationships taking shape, the regulated utility is being exposed to unprecedented outflows of cash and other assets while being saddled with new debt obligations in addition to those for the transferred assets. Therefore, special scrutiny is now required for these transactions.

(b) Parties' Positions

The marketers and OPC have been vociferous in their opposition to shared services. Enron/Statoil has stated that "to the extent some might consider, as a 'service', the offering of loans or guarantees by a utility to, or on behalf of, any utility affiliate, it should be clear that this kind of service is prohibited."[262] The Joint Commenters have noted with concern the reduced reliance on cost of service regulation and the substantially increased magnitude of utility debt obligations as reasons for not allowing a utility to guarantee the debt of an affiliate.[263] They conclude that "[T]hese risk factors outweigh any possible gain to Maryland consumers that would result from giving utility affiliates access to lower cost debt."[264] As for OPC, it argued that loans should reflect market rates (i.e., the credit standing of the affiliate on a stand-alone basis) and concludes that this requires a 25 basis point adjustment to the utility's credit rating.[265]

In this proceeding, Staff has addressed concerns raised by the Commission regarding the impact of loans and loan guarantees by a utility upon the regulated

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[262] Docket No. 60 at 23.
[263] Docket No. 61 at 19.
[264] *Id*.
[265] Docket No. 50 at 22.

operations of a utility.[266] Staff noted that volatile earnings, risky investments, mergers or takeovers, significant changes in the capital structure, and other factors can increase risks for a utility. Staff argues that "[T]he most direct and common result of increasing (business or financial) risk to a utility is an increase in the cost of capital."[267] "If the 'allowed' cost of capital (rate of return) is set to a higher value as a result of increased risk, utility rates must increase."[268] Staff noted that it is the Commission that has ultimate authority over rates generally, and the rate of return specifically. Staff asserts that if the allowed rate of return is significantly below the market cost of capital for an extended period of time, utilities will respond accordingly.[269] "That it, they will 'disinvest', allowing the system to slowly deteriorate, ultimately affecting the quality of service and safety."[270] However, it is the Commission's responsibility to assure service quality and safety. According to Staff, the necessary financing would have to come from equity or additional operating economies. Staff noted that if the parent company is healthy, this may not be a problem but if not, then "deterioration of the system could occur without some form of forceful intervention."[271] Staff noted that a utility may become a "cash cow" for a holding company that is in trouble.[272] Staff concludes that "as a result of the potential for increased risk and the resulting increase in rates, Staff recommends that the Commission consider some additional safeguards for ratepayers."[273] Staff noted that the federal government and other states have addressed these issues.[274] According to Staff, while the banking industry has been deregulated in recent years, federal legislation has

[266] Docket No. 105 at 10-22.
[267] *Id*. at 12.
[268] *Id*. at 13.
[269] *Id*.
[270] *Id*.
[271] *Id*.
[272] *Id*.
[273] *Id*. at 14.
[274] *Id*.

created safeguards or "firewalls" to prevent holding company finances from negatively affecting federally insured deposit companies.[275] For example, regulations provide access to holding company finances and the ability to require divestiture of depository institution subsidiaries under certain circumstances. "In addition, inter-affiliate activities are strictly limited, similar to our existing standards of conduct."[276]

Staff has described a number of Commission alternatives to respond where a utility requests an escalating rate of return as a result of company-specific risks. For example, the Commission may order a utility to restructure its debt or refinance in order to control capital costs. The Commission also might order a utility to cease any and all financial transactions with the holding company or any affiliates or consider further financial or legal separation.[277] Staff also suggests the institution of appropriate reporting requirements.

Staff foresees the regulated operations of utilities being overshadowed by unregulated businesses. Therefore, "as the utilities transform themselves into 'just wires' companies, the Commission may want to impose limitations (as a percentage [%] of total assets or of regulated debt for example at any one time) on that type of lending activity."[278] Staff claims that it will require certain oversight of loan activities for it to maintain information on the credit quality of a utility's cost of capital.

Staff argues that "[c]ontinuous support for multi-billion dollar ventures that rival or exceed the regulated utility's capitalization should not be condoned as prudent financial behavior."[279] In general, some type of separation is necessary."[280] Staff

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[275] *Id*. at 14-15.
[276] Id. at 15.
[277] *Id*. at 16.
[278] *Id*. at 18
[279] Id. at 19.
[280] *Id*., Staff noted that Florida Power & Light Co. is shielded from a non-utility affiliate, FPL Capital Group, Inc., and is not responsible for the latter's debt repayment.

indicates that one way to protect ratepayers is to permit utilities to use retained earnings as "seed money" for unregulated investments but prohibit recourse financing so that only the seed money, and not utility assets or future earnings, are at risk.[281] Staff argued that the large amount of debt incurred by affiliates of BGE and APS should be self-supporting now.[282] While the Commission has supported modest loan amounts in the past, Staff mentioned that "it is sheer hubris to expect any Commission to support credit supports (or debt) on unregulated investments gone bad or if the sum total exceeds the invested regulated capital, let alone many times that amount."[283] Staff concludes that utilities should exercise prudence in establishing a credit rating for its affiliates and that part of that process should be an annual utility filing that identifies which affiliates have credit guarantees or sponsorship and to what degree that exists.[284]

(c) Commission Decision

The Commission has given careful consideration to the financial relationship between utilities and their affiliates. Consistent with its policy to reject strict structural separation, the Commission declines to adopt the recommendation of the marketers that all loans and guarantees should be prohibited. However, this does not give the utilities a license to engage in imprudent activities or to jeopardize investments in utility services, maintenance or improvements. As both OPC and Staff have noted, certain rules and restrictions are appropriate.

The Commission determines that a utility shall not issue a loan or guarantee the debt of an affiliate if it creates a reasonable likelihood that the utility's cost of capital, credit worthiness or ability to provide regulated services will be adversely affected.

[281] *Id*. at 20-21.
[282] *Id*. at 20.
[283] *Id*. at 21-22.
[284] *Id*. at 22.

Loans should be from retained earnings only. Retained earnings should be used only when the utility is assured that its ongoing required investment in pipes, wires and other assets will be maintained at a sufficiently high level to assure continued safe, reliable and economical electric or gas service for its customers. A utility or affiliate, or any part of a consolidated company, should not assume that the Commission will automatically approve a loan by a utility or authorize any guarantee of an affiliate's debt. Guarantees of loans will be strictly scrutinized. Loans should be arranged on an arm's length basis, they should be set at fair market rates, they should include standard terms and conditions, and they should contain standard penalties for failure to repay the loan consistent with the stated terms and conditions.

In Case No. 8747, the Commission determined that:

> [a]pproval of loan guarantees may be granted 'upon a finding that to do so is consistent with the public convenience and necessity.' . . . If, subsequently, the loan guarantee has a negative impact upon a utility's credit standing, a corrective adjustment can be made in the utility's next base rate case. Thus stockholders, not ratepayers would bear the costs of any adverse effects on the cost of capital.[285]

The Commission will continue to look to stockholders to bear such costs. However, the concerns of the Commission extend beyond the application of risk in the setting of rates. Given the substantial shifts taking place in the structure and operation of the electric or gas companies, and their attendant affiliates, there is heightened awareness regarding the impact that loans and guarantees could have on the safety and reliability of utility service and the overall financial well-being of the regulated entity. Therefore, each gas or electric utility doing business in Maryland shall file with the Commission an annual

[285] 89 MD PSC 54, 81 (1998)

report that provides appropriate details of all outstanding loans and guarantees of debt by the utility. This report shall include the amount of debts, securities, loan, guarantees, terms of payment, call provisions, name of the corporate record keeper, credit agency analysis, issuance costs, default terms, and any other appropriate data necessary for this Commission to appropriately analyze these financial activities.

F. Reporting Requirements[286]

1. Parties' Positions

The utilities say that no new reporting requirements are necessary beyond those enumerated in Case No. 8747. Conectiv suggested that the Commission may request information as issues arise. It noted that the existing standards have been in existence for over 18 months and stated that to its knowledge, no evidence has been presented of any violation. Conectiv also argued that "reporting requirements should be developed on a case-by-case basis."[287] Pepco insisted that "Maryland utilities and their affiliates should not be required to bear the expense of, and competitive disadvantage associated with, an elaborate reporting and inspection scheme in the absence of some reason to believe that code of conduct violations will occur or, if they do occur, will likely go undetected."[288] Choptank stated that [F]or a Cooperative, additional costs are a large concern because increased costs deteriorate the money allocated to the member-owner."[289] Choptank noted that "a Cooperative has no shareholders to fall back on for excessive costs."[290]

[286] This section responds to Issue No. 10: What reporting requirements should be developed to demonstrate utilities are in compliance with standards of conduct?
[287] Docket No. 53 at 24.
[288] Docket No. 64, Attachment A, p. 3-4.
[289] Docket No. 70 at 7.
[290] *Id*. at 8.

Conectiv also noted that the Commission's existing complaint procedure is available. Columbia agrees with this point.[291]

WGL mentioned that "the relatively few complaints from the over 100,000 customers purchasing their gas from non-utility companies would indicate that the current standards and subsequent reporting requirements are working."[292] WGL argues that the purpose of reporting requirements is to "enable the Commission to determine whether the non-utility activities will affect regulated services, and to take timely steps to protect utility services, if necessary."[293] Chesapeake believes the use of cost allocation principles by the utilities requires the utility to monitor its own relationship with its affiliates to insure fair allocation and efficient management of costs. Reporting requirements to demonstrate that utilities are in compliance would be excessive and unnecessary."[294] Chesapeake asserted that issues can be addressed through a complaint procedure or as part of the next utility rate case.

NUI suggested that reporting requirements "should be based on regulator-determined materiality thresholds."[295] This will avoid unnecessary costs and burdens on the utilities and Commission. Further, the utility should keep sufficient records to enable the Commission to resolve any alleged improprieties. NUI generally advocates that utilities maintain CAMs.

The marketers generally prefer strict separation requirements, which they note eliminate the need for most reporting and compliance requirements. Alternatively, detailed reporting and CAMs are necessary. The Joint Commenters "recommend that the Commission adopt a relatively rigorous set of record-keeping, reporting and audit

[291] Docket No. 49 at 5.
[292] Docket No. 55, Appendix A at 4.
[293] *Id*. at 5.
[294] Docket No. 54.

requirements to apply for an initial three-year period, and re-evaluate the need for this information thereafter."[296] These records should include appropriate information regarding affiliate transactions and the maintenance of affiliate contracts and related bids. In addition, to the extent that FERC requires more detailed information or expeditious reporting, utilities must comply with FERC rules. The Joint Commenters recommend that for the first three years that these records be subject to an annual independent audit. They also say that such records should be available for third party review upon 72 hours notice. Finally, the Commission should reaffirm the disclosure and non-discrimination provisions adopted in Case No. 8747.

The Alliance has proposed a number of reporting and compliance requirements including: utilities must demonstrate their efforts to educate utility and affiliate personnel regarding the code of conduct and a continuing training plan; a CAM must be submitted to the Commission that sets forth appropriate allocation and pricing of shared services, personnel or assets approved by the Commission; utilities shall file compliance programs with the Commission annually; and Employee Transfer Reports shall be filed quarterly. The Alliance emphasized that these reports "must be publicly available."[297] The Alliance concludes that the Commission "must implement standards of conduct that eliminate to the greatest extent possible the need for the competitors of utility affiliates to police their compliance with Commission rules and regulations."[298]

Enron/Statoil noted that utilities should be required to demonstrate compliance with the standards of conduct by: incorporating affiliate standards into their tariffs; filing proposed implementation procedures with the Commission and all interested parties;

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[295] Docket No. 69 at 8.
[296] Docket No. 61 at 19.
[297] Docket No. 59 at 14.
[298] *Id*.

providing appropriate employee training; and filing annually (or within 15 days of a material change) a report identifying the corporate organizational structure, affiliated entities and the services performed, employees within each affiliate, and a disclosure of all services provided by the regulated utility to its competitive affiliates.[299] Additionally, the Commission should perform regular compliance audits and implement appropriate complaint procedures.

OPC supports substantial reporting requirements, including annual reports and concurrent reports.[300] Annual reports should cover the following areas: operational and organizational charts and information; allocations to affiliates of administrative, general, joint and common costs; reports of all affiliate transactions during the year; cash management transaction reports, including information or earnings, dividends, loans and other infusions of equity; and reports of all employee transfers. Concurrent reports should be filed shortly after a new affiliate is formed, containing basic organizational information and a description of new products and services and business objectives of the affiliate, plus compliance plans. OPC also stated that records of affiliates that transact business with the utility must be available for Commission audit and that the utility should itself have periodic audits conducted at shareholder expense.

Staff argued that "[T]he point of compliance is to ensure that the regulated entity, which has no competitors, is not subsidizing non-regulated affiliates or discriminating against non-affiliate companies in providing services."[301] Staff stated that within six months from the adoption of final standards, utilities should file appropriate compliance plans.[302] Plans should be filed annually thereafter, or within 90 days of any changes.[303]

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[299] Docket No. 60 at 23.
[300] Docket No. 50 at 23-27.
[301] Docket No. 73 at 11.
[302] Docket No. 51 at 19.

Staff strongly supports adoption of CAMs, which along with a code are "essential tools to ensure that ratepayers receive accurately priced products and services."[304] Staff requests that the Commission require utilities to "allow Staff complete and total access to all corporate books and records of the corporate organization that develop, verify and/or substantiate the reasonableness of all charges and allocations of costs to the utility and ratepayers."[305] Staff suggested this is necessary to assure that costs assessed to ratepayers are reasonable and equitable. Staff also recommends that utilities undertake, "at shareholder expense," an independent audit of their CAM at least once every three years, or upon a change in corporate structure, or when utility rates are revised.[306] Finally, Staff insisted that utilities should file annual reports of assets transferred during the year between the utility and affiliate. This will provide a "reasonable basis" to ensure that assets are transferred at appropriate values.[307]

2. Commission Decision

The Commission will require most energy utilities in the State to file Cost Allocation Manuals beginning with a CAM to be filed by no later than November 1, 2000. CAMs will be filed in accordance with the four cost allocation procedures previously adopted, [308] as well as the standards of conduct contained in this Order. The purpose of the CAM is to formulate the methodologies and procedures for the allocation of the costs of shared assets, employees and services between the utility and its affiliates.

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303 *Id*.
304 Docket No. 73 at 11.
305 Docket No. 51 at 20.
306 *Id*.
307 *Id*.
308 The four cost allocation principles are: allocations should be made on the basis of a fully distributed cost allocation methodology; the cost of services provided by a utility to its affiliate should be based upon the full cost of such services, including any indirect costs; the fair market value of services which reasonably could be marketed by a utility to the public must be allocated as the imputed cost to its affiliate; and transfers of assets between the utility and the affiliate should be based upon asymmetric pricing principles.

CAMs will serve as an aid in identifying the transactions that are actually taking place and will assist the Commission in verifying that appropriate methodologies are used and appropriate cost allocations are being made.

Although each CAM should be tailored to the specific circumstances of a given utility, the following elements are required:

- Corporate organization;
- Location of each corporate entity;
- Officers of each corporate entity;
- Index of operational and managerial employee units of the utility and each affiliate;
- Index of shared services; and
- Methodologies and procedures for cost allocations of services and asset transfers.

Changes to the CAM will require Commission approval.

While energy utilities will generally be required to file a CAM, the Commission finds that the record reflects that this requirement should not be applied to every gas or electric utility. Cooperatives, due to their particular structure, lack of generation facilities, and federal requirements are hereby exempted from filing a CAM. They are not exempted from the annual reports required below. Municipal utilities and Eastern Shore Gas Company, which are both exempted from this proceeding, are exempted from these CAM requirements. Likewise, a CAM may impose too much of a burden on small utilities. Therefore, any gas or electric utility doing business in Maryland with annual gross revenues of less than $20 million shall be exempted from filing a CAM. This will minimize the burdens on these smaller companies.

Case No. 8747 required each gas and electric company that filed a quarterly earnings report to file at the same time an affidavit that its cost allocations and transfer pricing of assets comply with the principles adopted in both Case Nos. 8577 and 8747. A requirement for affirming the accuracy of its cost allocation manual was also included. In addition to the other reports required herein, these reports and affidavits should be continued.

In general, gas and electric utilities are presently required to file annual reports in accordance with §§6-205 through 6-210 of the PSC Law. It is the expectation of the Commission that each utility will apply their CAM in determining the total revenues and total earned returns that are reported in the annual report. The purpose of these reporting requirements, among other things, is to facilitate Commission oversight of utility activities and ensure that utilities are complying with the appropriate cost allocation procedures and the various standards of conduct adopted in this proceeding. These allocation procedures and standards are being implemented to protect ratepayers, ensure the financial integrity of the regulated entity, and foster competition. Consequently, the Commission requires that the following additional information be included in the annual report:

- Complete descriptions of all affiliate transactions, including asset transfers;
- Complete descriptions of the utility services, including employees, shared with each affiliate;
- Complete description of all cash management transactions between a utility and any affiliate involving loans, securities, guarantees of debts or changes in capital structure;
- All information currently filed on FERC Form No. 1 if such information is not required by FERC after the date of this Order; and

- Descriptions of employee transfers from the utility to an affiliate or from an affiliate to the utility, including the employee's name, department, general responsibilities and duration of assignment.

The Commission is mindful of the independent audit requirement for cost allocation manuals contained in §4-208 of the PSC Law. In addition, each utility shall permit the Staff access to all books and records of the utility. The utility shall provide access or a copy of any necessary books and records to Staff in order to ensure that the utility is complying with the Orders of the Commission and that ratepayers are not subsidizing affiliate activities.

G. Promotional Practices[309]

1. Parties' Positions

Generally, the utilities take the position that the Promotional Practices Regulations ("PPRs") are an unnecessary competitive handicap and should be repealed. Consequently, they support unlimited discretion for utilities and affiliates to engage in such practices. Dr. Gordon recommends "that these rules be rescinded in their entirety, since they have been superseded by subsequent commercial and regulatory events (especially Order No. 74038)."[310] He argued that the Commission "has sufficient tools to address the legitimate regulatory concern of preventing utilities from subsidizing their affiliates."[311]

[309] Issue No. 14: Should the Commission's Promotional Practices Regulations, codified as Subtitle 40 of Title 20 of the Code of Maryland Regulations, be revised? Issue No. 15: How and to what extent, if any, should utilities and/or their affiliates be permitted to engage in promotional practices as currently defined to offer incentives, rebates, or other promotions, including but not limited to, demand-side management to encourage the use or sale of electricity in any form? Issue No. 11: When should the details of a utility's proposed promotion be filed with the Commission? Issue No. 16: What requirements and restrictions should govern the relationship between utilities and their affiliates in communications, marketing, and permissible promotional practic es?

[310] Docket No. 56 at 22.

[311] *Id*.

BGE supports Dr. Gordon's positions.[312] BGE asserts that "the Commission's transfer pricing rules, cost allocation principles and Cost Allocation Manual already prevent subsidies from BGE to its affiliates."[313] In addition, BGE suggested that the Commission has sufficient audit and ratemaking authority over the utility to protect ratepayers from inappropriate promotional expenditures.[314]

Pepco argued that the PPRs are anti-competitive "to the extent they limit the activities of Maryland utility affiliates while imposing no restrictions on out-of-state competitors."[315] According to Pepco, joint promotions should be allowed as long as affiliates bear their own fair share of the cost of such promotions and comply with all other code of conduct requirements.[316] Pepco emphasizes that the PPRs should be repealed because they were designed to suppress competition between electric and gas utilities, which is no longer compatible with the pro-competitive orientation of current State policy.[317] According to Pepco, "other market participants will be well-situated to detect any violations and call them to the Commission's attention."[318] Pepco recommends that the Commission rely on consumer protection regulations to be implemented under the Act rather than the "outdated" PPRs to guard against abuses.[319] Pepco also argued that if the PPRs are not repealed, then the Commission should eliminate their applicability to non-residential customers and rule that the PPRs do not apply to activities of utility affiliates in a competitive market.[320]

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312 Docket No. 57 at 7.
313 *Id*.
314 *Id*.
315 Docket No. 64, Attachment A at 5.
316 *Id*. at 6.
317 *Id*. at 5.
318 *Id*. at 4.
319 *Id*.
320 *Id*.

Conectiv stresses that as long as below-the-line dollars are used, there should be no restrictions, including promoting the sale of electricity or DSM measures.[321] Only if the costs of a utility promotion will be captured "above-the-line" should it be filed with the Commission.[322] If the PPRs are not rescinded, "the Rules should be amended to clarify that non-jurisdictional activities performed by affiliates are not subject to such Rules."[323] Conectiv says that marketers might try to use the PPRs as a "sword" to assert that any retail marketing activity of an affiliate is a "promotional practice." This would require the affiliate to show that its marketing activity is a just and reasonable business practice and is calculated to benefit the utility and its customers.[324] Conectiv requests that the Commission reconsider its requirement for utilities to inform the Commission of new non-utility activities on a time-concurrent basis and the level of assets committed to the venture. According to Conectiv, "[D]isclosure of individual investments in non-utility activities would competitively disadvantage Maryland utilities."[325] This is proprietary, commercially-sensitive information that competitors not subject to Commission jurisdiction will not be required to reveal. Conectiv says that reporting the aggregate investment in such activities annually would be preferable. In addition, if every new investment in non-utility activities must be reported, it will likely require hiring personnel solely to comply with this requirement. Conectiv noted that the PPRs require that details of a promotion must be filed 30 days in advance of issuance. Conectiv says that "[N]o participant in a competitive market should be required to disclose its marketing plans to competitors 30 days in advance of execution of those plans

[321] Docket No. 53 at 32.
[322] *Id*. at 25.
[323] *Id*. at 30.
[324] *Id*. at 31.
[325] *Id*. at 26.

or to perform and disclose its analysis of the costs and benefits of such plans."[326] Conectiv also points out that COMAR 20.40.01.02(F) may be interpreted to prohibit a utility affiliate from packaging two competitive products if one product is offered below cost.[327] Conectiv says non-utility affiliates would not be barred from making such package offers.[328]

Columbia says the PPRs are no longer needed and should be rescinded.[329] "They are inappropriate in today's highly competitive energy markets, and place utilities and their affiliates at a competitive disadvantage because they do not apply to other participants in the market."[330] In particular, Columbia argues that "the standards adopted in Order No. 74038 should be modified to permit utilities to engage in joint advertising, sales calls, and other promotional activities with their affiliated energy suppliers if they are willing to engage in similar activities with unaffiliated suppliers under the same terms and conditions.[331]

NUI says that "[N]either a utility nor its affiliate should be discouraged from participating in a market, particularly in the demand side management area where efficient utilization of energy is encouraged."[332] NUI concludes that because the PPRs have this "discouraging effect" they are "completely outdated."[333] However, NUI argues that it would be reasonable to file proposed promotions 30 to 60 days in advance, on a confidential basis, with implementation at the end of this period.[334]

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[326] *Id*.
[327] *Id*. at 31-32.
[328] *Id*. at 32.
[329] Docket No. 49 at 5-6.
[330] *Id*. at 5.
[331] *Id*. at 6.
[332] Docket No. 69 at 11.
[333] *Id*.
[334] *Id*. at 10.

Chesapeake says the PPRs should be modified to exclude their application to affiliates "because it exceeds the jurisdiction of the Commission to directly regulate the promotional activities of unregulated affiliates."[335] Chesapeake also says that the definition of "public utility" or "person" under COMAR "should include gas marketers and suppliers because they should be subject to the same standards as the regulated utility and its core service affiliates."[336] Chesapeake says that "[A]s long as no harm comes to the ratepayers . . . the standards of conduct adopted in Case No. 8747 should be sufficient to monitor promotional practices, including incentive and rebate offers, and any promotion to encourage the use of the utility's regulated energy source, like demand-side management promotions."[337] The Commission "could monitor promotional practices through the utility's code of conduct and cost accounting principles."[338] Chesapeake concludes that annual reporting can provide the Commission with the information necessary to protect ratepayers from potential harm that could result from public utility diversification.[339]

WGL takes a different position than most other utilities. WGL "believes that the PSC's Promotional Practice Regulations should not apply to an affiliate of a public service company. Otherwise, the regulations should remain in effect."[340] WGL says the reasons for this are: 1) "the focus and approach to regulating public service companies have changed dramatically since the regulations were first adopted in 1970" and 2) "the Commission's jurisdiction over the activities of unregulated affiliates is highly questionable."[341] Further, non-jurisdictional utility affiliates are not subject to a

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335 Docket No. 54.
336 *Id*.
337 *Id*.
338 *Id*.
339 *Id*.
340 Docket No. 55, Appendix A at 6.
341 Docket No. 55 at 6.

prohibition against promotional offerings. According to WGL, "lifting of the restrictions on an affiliate while retaining the restrictions on the regulated entity will foster the economic use of energy sources without ratepayer subsidies.[342] WGL concludes that as long as affiliate costs are not subsidized by ratepayers, any further action is beyond the Commission's jurisdiction.[343]

The marketers take a strict view of promotional practices. The Alliance takes the position that "promotions by regulated utilities should be prohibited entirely and the Promotional Practices Regulations repealed."[344] Therefore, promotional filings are unnecessary. The Alliance claims that the PPRs have been routinely ignored. Therefore, if they are retained, they should be enforced.[345] In addition, it says "[U]tilities must also be precluded from engaging in merchandising, service and repairs, and providing various equipment, appliances and material."[346] However, affiliates should not be precluded from offering manufacturer incentives and rebates.[347] The Alliance argues that because utilities' sole function will be to deliver electricity, "there is simply no justification for permitting utilities . . . to engage in promotional practices for conservation, energy efficiency, or to promote the use of electricity, or to engage in any other non-distribution related activity."[348] "These are functions of the competitive market, not monopoly utilities."[349]

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[342] *Id*., Appendix A at 6.
[343] *Id*. at 8.
[344] Docket No. 59 at 19.
[345] *Id*.
[346] *Id*.
[347] *Id*. at 16.
[348] *Id*. at 20.

Enron/Statoil says that revision of the PPRs "should be addressed only after first attending to the necessary revisions and additions to the standards of conduct."[350] Enron/Statoil argues that if a service can be provided competitively by an entity other than a utility, then the utility should not be offering a promotion, unless the incentive is targeted to its distribution business, its distribution customers can receive the incentive regardless of their electricity supplier, and the incentive is applied as a distribution cost savings to the customer.[351] Enron/Statoil advocates "a prompt Staff review process for any utility promotions to ensure compliance with the prohibition against the marketing of standard offer service, and with the necessary disclaimer requirements.[352]

MAPSA says that the PPRs are old, have stagnated, and largely been ignored.[353] In addition, "the markets in which they purport to operate in and regulate have changed dramatically."[354] Now that electric service is to be competitive, "the promotion of energy efficiency, energy efficient appliances and equipment, and conservation programs appropriately belongs in the competitive market."[355] MAPSA argues that "[U]tilities should only be delivering energy."[356] Once utility participation in these programs is prohibited, then the PPRs should be repealed, MAPSA says.[357]

The Joint Commenters urge the Commission to "restrict the utilities themselves to providing Standard Offer Service and . . . prohibit any promotions of such service."[358] Therefore, affiliates should not be prohibited from engaging in promotional practices.

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[349] *Id*.
[350] Docket No. 85 at 29.
[351] Docket No. 60 at 25.
[352] *Id*. at 24.
[353] Docket No. 63 at 12.
[354] *Id*.
[355] *Id*. at 12-13.
[356] *Id*. at 13.
[357] *Id*.
[358] Docket No. 61 at 24.

However, all promotions should comport with code of conduct provisions. The Joint Commenters say that utilities should file the details of proposed promotions "with sufficient lead time to allow for review and amendment as needed to comply with the code of conduct."[359] They suggest 30 days. They argue that this recommendation "strikes a balance between the utility's legitimate desire to respond in a timely manner to market conditions and the public interest in ensuring that utility promotions do not undermine the development of competition."[360] "To the extent that the utility still administers any demand-side management programs, it is especially important that the Commission apply the non-discrimination provisions."[361]

OPC says "affiliates should be allowed to engage in most promotional practices to sell their services without either regulation or requirement that promotional plans be filed with the Commission."[362] According to OPC, this puts utility affiliates on the same footing as other unregulated energy service companies. However, OPC recommends two restrictions on affiliate promotional practices: "1) They should be prohibited from discounting or repackaging services offered by the regulated utility to prevent customer confusion and unfair marketing; 2) To the extent that they are permitted to advertise their affiliation with the utility in any way, they must clearly state in promotional materials that they are not part of the regulated utility and that customers need not contact them to obtain utility service."[363] As for the regulated utilities, OPC says that they should "not be allowed to advertise, except for advertising related to safety and the offering of energy conservation and low income assistance through public benefits programs."[364] OPC says

[359] *Id*. at 21.
[360] *Id*.
[361] *Id*. at 25.
[362] Docket No. 50 at 31.
[363] *Id*.
[364] *Id*.

DSM programs funded through a public benefit surcharge should not be provided by utilities in the long run, if possible.[365] OPC asserts that if the utility is the service provider, it should be required to provide a disclaimer "that DSM programs will be made available to all wires customers, regardless of their retailer and that customers do not have to purchase electric energy either from the utility as default service or from the utility's affiliate to be eligible for these programs.[366] Utilities should also be permitted to provide factual information requested by customers as required by the Commission.[367] OPC says it is reasonable for a utility to file a schedule of promotional practices 30 days before beginning a promotional campaign. OPC emphasizes that utilities should no longer be permitted to promote appliance retailing, rental and service guarantee activities. Therefore, utilities would have to spin off these activities to affiliates.[368] OPC's recommended changes will require certain one-time filings by utilities.[369]

"Staff recommends that the existing Promotional Practice Rules in COMAR be repealed."[370] According to Staff, "the nature of the regulated utility will likely be one of a smaller business entity in a large group of unregulated generation and marketing businesses, perhaps within a holding company umbrella."[371] In a holding company structure, the regulated wires company only has an indirect interest in helping maximize the output of its sister affiliates."[372] "Thus, it would seem to follow that the incentive to sell the utility's generation solely into the former native load market does not exist as strongly as it used to."[373] Therefore, Staff concludes that the PPRs are "no longer

[365] *Id*.
[366] *Id*.
[367] *Id*.
[368] *Id*.
[369] *Id*. at 28.
[370] Docket No. 51 at 23.
[371] *Id*. at 22.
[372] *Id*.
[373] *Id*.

appropriate within the context of the emerging deregulated arena, and should be repealed within the transition period."[374] If a distribution company wants to present a particular service offering to customers, then it should be required to tariff that offering consistent with Commission regulations, Staff says.[375] Staff noted that affiliates can be expected to make unique customized offers to consumers to be competitive with marketers. The current PPRs would restrain this activity, thereby restraining the market and its creativity.[376] Staff noted that DSM programs are designed to promote conservation and more efficient uses of resources.[377] Staff concludes that "there is no reason to prevent the promotion of electricity use (or gas use for that matter) in any form, by distribution utilities and affiliates.[378] Staff also concludes that "[R]estructuring all of Maryland's formerly regulated energy markets creates a different situation for all competitors which requires very little promotional practice oversight from this Commission."[379]

2. Commission Decision

The Commission notes approvingly the general agreement of all parties that the PPRs should no longer be applied to utility affiliates. The Commission agrees that in a competitive marketplace it is inappropriate to require affiliates to abide by the PPRs when other competitors do not have to comply with these regulations. Application of the PPRs to affiliates creates an unnecessary competitive handicap for the affiliates.

The utilities (except for WGL) and Staff support complete repeal of the PPRs. This would result in no promotional practices restrictions being applied to the utilities and would allow them to freely promote their services. The marketers and OPC argue

[374] *Id*.
[375] *Id*.
[376] *Id*. at 23-4.
[377] *Id*. at 24-25.
[378] *Id*. at 25.
[379] *Id*.

strenuously that the only services the utilities should provide is their regulated transmission and distribution services. Therefore, they say that the PPRs can be totally repealed because utilities should be completely prohibited from engaging in promotional practices.

The Commission concurs with the parties and will exempt affiliates from the PPRs. However, the Commission will take a more moderate approach regarding the regulated utilities. The Commission will undertake a review of COMAR 20.40 in due course to determine whether those regulations should be repealed or revised. In the meantime, the Commission notes that § 4-503(b) of the PSC Law prohibits a utility from using special rates, rebates, drawbacks, or refunds to treat persons of similar circumstances differently, or to give undue preference to a person, locality, or class of service. Additionally, the Commission notes that this Order establishes prohibitions on the marketing of Standard Offer Service and on joint promotions of a utility and an affiliate.

The Commission also wishes to make clear that the utilities will be permitted to promote energy conservation, energy efficiency, and the use of electricity or gas within the confines of these constraints. The following disclaimer must be provided by the utility if it provides DSM services:

> DSM programs (fill in the specific program if applicable) are available to all distribution customers, regardless of their generation supplier. Customers do not have to purchase electric energy either from (fill in the utility's name) or from any affiliate to be eligible for these programs.

Finally, a request by a utility to engage in any promotional practice must be filed with the Commission at least 14 calendar days before the proposed promotion is to begin.

H. Name and Logo[380]

1. Parties' Positions

The utilities generally take the position that minimal disclaimers are appropriate when an affiliate uses the utility's name or logo. In addition, they argue that affiliates should neither be banned from using the name or logo of the utility or be required to pay a royalty for such usage. Not surprisingly, the marketers argue that affiliates should be prohibited from using the utility's name or logo. In the alternative, they support the imposition of a royalty. OPC supports the marketers on this issue. The AG-CPD favors a ban. Staff recommends that comprehensive disclaimers be adopted. No issue in this proceeding has generated more controversy.

Dr. Gordon, testifying on behalf of several utilities, stated:

> From an economic perspective, the only reason to require a disclaimer is to alert the potential customer to the fact that it is not dealing with the utility. Such a notice does not require an extensive disclaimer and to create a requirement for an extensive disclaimer only raises costs to one set of competitors, thereby providing the non-affiliated competitors with a cost advantage.[381]

In addition, he says that the affiliate's roots in the regulated company "are a major source of any legitimate competitive advantage the affiliate may possess."[382] Dr. Gordon says that permitting affiliates to use the same or similar names and logos is beneficial to consumers because it provides "information on who they are dealing with at a time when many regulators and state legislatures are funding consumer education programs and generally searching for ways to help consumers adjust to the new gas and electricity

[380] This section analyzes Issue No. 13. What disclaimers should be provided to detail the relationship between a utility and its affiliate or between an affiliate and parent?
[381] Docket No. 56 at 20.
[382] *Id*. at 21.

markets."[383] He argues that clear brand identification encourages accountability and provides an incentive for firms to maintain high levels of quality and service. Dr. Gordon concludes that "[E]liminating the apparent connection with the incumbent will give a windfall to new entrants but it will do nothing for customers."[384] Dr. Gordon also says that requiring affiliates to pay royalties when they use the utility's name or logo "is an unreasonable policy with no basis in the economics of either competitive or regulated markets."[385] Royalties "simply create a transfer from the affiliate to the utility."[386] Dr. Gordon also claims that "there is no objective, practical means for setting royalty payments."[387]

Pepco says that in Case No. 8747, the Commission determined that an affiliate may use a utility's name or logo provided that there is no representation that an advantage accrues to customers as a result of dealing with the affiliate. The Commission also determined that a prominent disclaimer that the utility and affiliate are separate entities must be displayed. Pepco says there "is no need for additional disclaimer requirements."[388] Pepco also says that restrictions on names/logos are bad policy because "utility brand names and logos are an effective means of conveying truthful information to consumers."[389] Pepco argues that "[o]wners of brand names and logos also have a powerful incentive to maintain the value of the brand/logo by maintaining high standards, which also ultimately redounds to the benefit of consumers."[390] Pepco says that while some parties have argued that consumers will be confused by shared trade names and

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[383] *Id*.
[384] *Id*.
[385] Docket No. 79, Reply Testimony of Kenneth Gordon at 24.
[386] *Id*.
[387] *Id*.
[388] Docket No. 64, Attachment A at 4-5.
[389] Docket No. 106 at 16.
[390] *Id*.

logos, no evidence supports this proposition. "Customer confusion is unlikely to be a problem where adequate disclaimers are in place to guard against deceptive practices, as they are in Maryland," says Pepco.[391] Pepco says that not all utilities have favorable reputations and that utilities that do "have earned that goodwill by providing high quality service."[392] As for royalties, Pepco noted that "no utility has ever included this so-called goodwill asset in rate base and received a rate of return on its value."[393] Further proponents of royalties have not presented a viable means of valuing a utility's name/logo. Pepco also points out that most neighboring stated freely permit names/logos to be shared, "subject only to reasonable disclaimer requirements."[394] Pepco concludes that if Maryland adopted harsher policies, it would simply harm local utilities and give competitors an unfair advantage.

As for disclaimers, "Pepco has reservations concerning the much-discussed proposal to add new language to the existing disclaimer, which indicates that utility affiliates are not regulated by the Commission."[395] Pepco says it appears that some parties want to create the impression that utility affiliates are completely unregulated and "somehow more dangerous to do business with than non-utility affiliates."[396] According to Pepco, all unregulated entities should indicate this status or there may be an implication that companies that do not have the disclaimer are regulated. Pepco also argues that "[l]engthy disclaimer requirements impose heavy costs on utility affiliates" and that "the Commission should avoid overly complex language that will have little meaning to most consumers."[397]

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[391] *Id*. at 17.
[392] *Id*.
[393] *Id*.
[394] *Id*. at 18.
[395] *Id*. at 20.
[396] *Id*.
[397] *Id*.

APS supports the agreement reached in its restructuring settlement. Pursuant to it settlement Affiliate Code of Conduct, Section IV provides:

> A. Disclaimers. Whenever a Utility affiliate provides written or printed mass marketing materials to the public using the Utility's name or logo, it shall include a disclaimer that states that the affiliate and the Utility are not the same business and that the affiliate is not a regulated utility.[398]

APS says that its settlement disclaimer "requires disclosing the most vital information, that the affiliate and the utility are not the same business."[399] APS says the most serious concern was that affiliate use of the name/logo might be viewed as a deceptive trade practice. However, APS says that "[T]he simple truth is that it is bad policy to bar a customer from receiving accurate information with which to make a decision in a competitive marketplace, especially a marketplace which is just opening up."[400] If there is any deception, APS says that the AG-CPD "will be on top of it."[401] Further, the real reason, according to APS, that some parties want affiliates to pay a royalty is to raise the price of affiliate services so that potential competitors can undercut these prices. Artificially raising prices is not the way a competitive market should work, says APS. APS concludes that it would be appropriate for the Commission to adopt the disclaimer from its settlement.

Conectiv agrees with the Commission's previous position that affiliates should be permitted to use the utility name/logo. However, Conectiv "disagrees that a disclaimer should be required."[402] Conectiv says the name and logo are corporate assets that do not belong to customers. The Company says that if a disclaimer is required, "it should only

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[398] Docket No. 46 at 3.
[399] Docket No. 96 at 9.
[400] *Id*. at 10.
[401] *Id*.
[402] Docket No. 53 at 28.

apply to energy marketing activities for all of the same reasons that it is appropriate to have different sets of standards for core-service and non-core-service affiliates."[403] Further, Conectiv says the disclaimer should be adaptable to cover competitive "below the line" activities that from a legal standpoint are performed within the corporate utility structure. Conectiv also requests that the Commission clarify whether the disclaimer would be required in connection with the use of "a related but clearly distinguishable name (i.e., Conectiv Communications versus Conectiv Power Delivery)."[404] Lastly, Conectiv says a disclaimer should be limited to mass media or printed solicitation materials of general circulation.

Conectiv says that it specifically objects to any restrictions or imputed royalties on the use of the Conectiv name or logo. "Conectiv has expended considerable below-the-line resources developing its relatively new brand."[405] Conectiv says it has embarked on an "umbrella brand" strategy. It argues that Maryland law prohibits false claims of affiliation, not truthful ones. The name, brand and reputation belong to Conectiv and its shareholders, the Company claims. "Common branding also is important to realizing economies of scope."[406] Conectiv says that with a common brand, there is an incentive to improve and maintain quality service, "including the market in which it has franchised transmission and distribution operations, in order to maintain the value of the brand."[407] Lastly, if the Commission adopts a disclaimer, it should use the one adopted in Case No. 8747. However, it should be clarified that this disclaimer only applies to energy marketing affiliates within the franchised service territory of the utility.[408]

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[403] *Id*. at 29.
[404] *Id*.
[405] Docket No. 74 at 10.
[406] *Id*. at 11.
[407] *Id*. at 12.
[408] *Id*. at 13.

Conectiv makes a point of arguing that it "is differently situated with respect to the use of the name and logo of Conectiv and derivatives of that name and logo for the businesses under Conectiv."[409] Neither Conectiv Power Delivery ("CPD"), the regulated utility, nor any of the other businesses will be using the old utility name, "Delmarva Power." "Over approximately the last two years, the new name Conectiv was created and substantial sums were spent . . . on creating a new image for Conectiv's various businesses under the new name and logo. All of the dollars spent advertising the new name and image, and creating and developing the new logo, were below-the-line shareholder dollars."[410] Conectiv says that even if the Commission adopts restrictions for "well-established" utility names and logos, "any such new rule should exempt distinct names and logos, such as Conectiv's, that have been in use less than three years."[411] Conectiv concludes that a ban on the use of the Conectiv name or logo, or a royalty requirement, will only "hamper its ability to compete but would serve no public interest."[412]

BGE and Conectiv also submitted the testimony of Jeffrey H. Howard, Esq., an antitrust law expert.[413] Mr. Howard says that there "is certainly no need to absolutely bar the use of a common name or logo to achieve any of the policy goals established in §§ 7-504 and 7-505(a)."[414] He argues that a prohibition constitutes competitive handicapping, which is anti-competitive, anti-consumer, and inconsistent with the Act. Mr. Howard says that name recognition and reputation is one of the significant areas where a firm can take advantage of economies of scale and scope. He says many competitive firms enjoy

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[409] Docket No. 97 at 7-8.
[410] *Id*. at 8.
[411] *Id*.
[412] *Id*.
[413] Docket No. 79, Reply Testimony of Jeffrey H. Howard, Esq.
[414] *Id*. at 35.

these same efficiencies. Mr. Howard concludes that it would be "highly anti-competitive and anti-consumer to allow large competitors to take advantage of these economies while barring Maryland's utility industry from doing the same."[415] Mr. Howard also claims that surveys indicate that consumers: support the continued sale of electricity by the utility or its affiliate; feel it's important to know the owner of their electric power; generally oppose regulatory limits on affiliate use of utility names; favor rules that permit utilities to provide information concerning their affiliates, and generally support the use of utility names and logos by affiliates.[416] Mr. Howard concludes that if affiliates are not allowed to use utility names and logos, consumers lose information on who they are dealing with and their search costs are raised. In addition, "if consumers are denied brand identity for utility affiliates, they may in fact be confused about the ownership of the affiliate."[417] Mr. Howard says that to the extent disclaimers are required, they should be limited to commercial advertising. Finally, he says that the "advocacy of royalties is simply another way for competitors to raise their rivals' costs."[418]

BGE and Conectiv also filed Joint Final Comments herein.[419] They say that the Commission should reject a ban on a common name and logo because it is unnecessary, it is anti-consumer, it would violate First and Fifth Amendment rights, and other state commissions have consistently rejected such bans.[420] BGE and Conectiv say a ban does not advance the goals of the Act because: any name value belongs to shareholders, therefore use by an affiliate is not a ratepayer cross-subsidy; a ban would artificially raise a Maryland company's costs; and it would limit customer information. Ratepayers, BGE

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[415] *Id*. at 36.
[416] *Id*. at 37.
[417] *Id*. at 38.
[418] *Id*. at 39.
[419] Docket No. 102; Joint Final Comments Brief of Delmarva Power & Light Company d/b/a Conectiv Power Delivery and Baltimore Gas and Electric Company.

and Conectiv say, have no property interest in the name or logo because they have not subsidized any value that may be attached to these assets. In addition, "if consumers are denied brand identity for utility affiliates, they may in fact be confused about the ownership of the affiliate."[421] BGE and Conectiv also question the intent of some of Enron/Statoil's suggested disclaimers. BGE and Conectiv say that if Enron/Statoil's disclaimers are adopted, they should apply to affiliates and marketers alike. BGE and Conectiv claim that "virtually every state commission that has adopted a Code of Conduct for energy deregulation has declined to impose the outright ban urged by the Alliance here."[422] Moreover, FERC has adopted Codes of Conduct regarding electric transmission and natural gas sales and these codes are "narrowly circumscribed to address only the legitimate issues of open access and cross-subsidization."[423]

BGE has also submitted a proposal for "Recommended Disclaimer Procedures" to be applied to BGE and any of its affiliates that use the BGE name or logo.[424] BGE says the proposal is not for application to other Maryland utilities.[425] However, one disclaimer would apply to all marketers selling to end-use customers in Maryland.

BGE Home Products and Services, Inc. ("BGE HOME") also filed comments regarding the use of names and logos by an affiliate as well as the use of disclaimers.[426] "BGE HOME strongly urges the Commission to reject any unfair recommendations concerning either a ban on the use of a common name/logo, or the imposition of a

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[420] *Id*. at 14-15
[421] Id. at 17.
[422] *Id*. at 18.
[423] *Id*. at 18-19.
[424] Docket No. 102; Final Comments of Baltimore Gas and Electric Company, (Attachment A).
[425] *Id*. at 3.
[426] Docket No. 102, Final Comments of BGE Home Products and Services, Inc.

royalty. These extreme measures will harm many customers by creating significant confusion and substantially driving up marketing and advertising costs."[427] BGE HOME claims that it "has invested nearly $24 million in both advertising and branding activities, which have enabled the Company to create its own distinctive identity."[428] In its Final Comments, BGE HOME has proposed "enhanced and specific disclaimer language" which it says will cost BGE HOME "in excess of $250,000 annually."[429] BGE HOME claims, among other things, that a ban or royalty: may degrade its "superior service;" "may result in the potential destruction of economic and employment growth which we have fostered; will certainly create more customer confusion and complaints; and, will potentially cause the exporting of a significant local tax and employment base to firms located outside the State of Maryland."[430] BGE HOME says branding is a necessity in today's marketplace: and that many competitors are "national in name recognition."[431] BGE HOME says that "use of a new and fictitious name for BGE HOME . . . would cause significant confusion among our many loyal customers," "artificially raising advertising and marketing costs" which "would inevitably be passed onto Maryland consumers."[432] For all these reasons, BGE HOME urges the Commission to reject a ban or require a royalty for use of a common name/logo.

In addition to the policy arguments raised by the utilities for not imposing a ban or royalty on affiliate use of utility names and logos, they also argue that Constitutional restraints prohibit the Commission from taking such action. Conectiv says that "advertising is protected under the First Amendment as commercial speech."[433] Conectiv

[427] *Id*. at 3.
[428] *Id*.
[429] *Id*. at 3-4. See Attachment A for the disclaimer language and matrix.
[430] *Id*. at 7-8.
[431] *Id*. at 8.
[432] *Id*. at 9.
[433] Docket No. 53 at 28.

says that any prohibition on advertising must be a reasonable time, place or manner restriction, a permissible subject matter regulation, or a narrowly tailored means to serve a compelling state interest or the prohibition is a violation of freedom of speech under the First Amendment.[434] Conectiv and BGE argue that the First Amendment "prevents this Commission from restricting truthful commercial speech, which includes the choice of the affiliate's name."[435] "Even in monopoly markets, the suppression of advertising reduces the information available for consumer decisions and thereby defeats the purpose of the First Amendment."[436] Conectiv and BGE also say that such a ban would constitute an illegal prior restraint.[437] They also state that "the Supreme Court has consistently recognized that regulations that ban a particular use of private property and do not substantially advance legitimate state interests constitute a taking without just compensation in violation of the Fifth Amendment."[438]

Perhaps the most forceful advocate of the Constitutional arguments has been Pepco.[439] Pepco says that the First Amendment, as applied to the stated through the Fourteenth Amendment, protects "commercial speech" from unwarranted restrictions. It says the Supreme Court has defined commercial speech broadly to include trade names.[440] Other courts have emphasized that product labels and trade names provide important information worthy of constitutional protection.[441] Pepco says the "cornerstone of the Supreme Court's commercial speech jurisprudence is *Central Hudson*

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[434] *Id*.
[435] Docket No. 102, Joint Final Comments of Conectiv and BGE at 17. See *Consolidated Edison Co. v. Public Serv. Comm'n,* 447 U.S. 530, 543 (1980).
[436] *Id*. at 17-18 quoting *Central Hudson* at 567.
[437] *Id*. at 18. See *Nebraska Press Ass'n v. Stuart*, 427 U.S. 539, 559 (1976).
[438] *Id*., citations omitted.
[439] Docket No. 106 at 10-15.
[440] *Id*. at 10. See *Virginia State Bd*. 425 U.S. 748, 762 (1976).
[441] *Id*. at 10-11.

Gas & Electric Corp. v. Pub. Serv. Comm'n of New York ("*Central Hudson*"),[442] which held that a regulation completely banning promotional advertising by an electric utility violated the First Amendment."[443] According to Pepco, *Central Hudson* uses a four-part analysis for reviewing regulations that restrict commercial speech. First, the court must determine if the speech at issue is misleading or pertains to unlawful activity, in which case it is not entitled to protection. Second, the government is required to show a substantial interest in the challenged regulation. The regulation must also directly advance the asserted governmental interest. Lastly, the regulation must not be more extensive than necessary to serve the government's substantial interest.[444] Pepco concludes that the restrictions on names/logos proposed in this proceeding "fall far short of satisfying the *Central Hudson* test. Pepco asserts that "it is not misleading for a utility affiliate to use the utility's trade name or logo, especially when adequate disclaimers . . . are in place."[445] Pepco says that affiliate use of a utility's trade name/logo "is a legitimate competitive advantage derived from years of reliable, responsive service and [is not] . . . unlawful for purposes of the first prong of the *Central Hudson* test."[446] Pepco says courts are hostile to "paternalistic efforts to protect consumers from truthful information on the ground that it might confuse them" and therefore, restrictions on the use of trade names and logos would likely fail the second prong of *Central Hudson*.[447]

Pepco says that to satisfy the third prong of *Central Hudson*, the government must show that "the harms it recites are real and that its restriction will in fact, alleviate them to a material degree."[448] Pepco argues that to justify restrictions, the government would

[442] 447 U.S. 557 (1980).
[443] Docket No. 106 at 11.
[444] *Id*. at 11-12.
[445] *Id*. at 12.
[446] *Id*. at 12-13.
[447] *Id*. at 13.
[448] *Id*., See *Edenfield v. Fane*, 507 U.S. 761, 770-71 (1993).

have to show that they promote competition, prevent cross-subsidization and avoid consumer confusion, when the opposite is true.[449] As for the fourth prong of *Central Hudson*, Pepco asserts that the goals sought to be achieved "can be met without burdening First Amendment rights, through open-access requirements, regulatory oversight of the utility-affiliate relationship and the adoption of reasonable disclaimers."[450] According to Pepco, there is no need for new regulations because these elements are already in place in Maryland.[451]

According to Pepco, content-based restrictions on speech are subject to "strict scrutiny" and "will be struck down unless they are the least restrictive means of advancing a compelling state interest."[452] Pepco says that a prohibition on an affiliate's use of a utility name/logo "would be a content-based restriction because it would effectively bar any communication to the public concerning the utility-affiliate relationship, as distinct from all other subjects."[453] Pepco concludes that consumers "can be just as effectively protected by disclaimers and consumer education programs."[454] Lastly, Pepco argues that "a rule prohibiting utilities and their affiliates from using the same logo and trade name would constitute a taking of utility property under the Fifth and Fourteenth Amendments which would necessitate the payment of just compensation."[455]

WGL says there is no factual basis in this proceeding to justify a ban on affiliate use of a utility's name/logo.[456] Therefore, WGL recommends that the Commission await

[449] *Id*.
[450] *Id*. at 14.
[451] *Id*.
[452] *Id*. at 14, See *Perry Educ. Ass'n v. Perry Local Educators' Ass'n*, 460 U.S. 37, 45 (1983).
[453] *Id*. at 14-15.
[454] *Id*. at 15.
[455] *Id*.
[456] Docket No. 101 at 8.

more experience with the practices of affiliates and competitors before considering such action.[457]

WGL's position is as follows:

> Marketing literature provided by utility affiliates should contain a disclaimer by the affiliate to assist in increasing customer understanding of the affiliate being a separate entity from the utility. The disclaimer should indicate that the utility and affiliate are separate entities. The marketing literature should not represent that any advantage would accrue to customers from the utility in the selection of the affiliate for a particular service.[458]

Further, "the Commission should reaffirm the Case No. 8747 ruling regarding the use of a utility's name and logo."[459] WGL says that claims that ratepayers have an equity interest or have established any goodwill that the utility name or logo may have are incorrect. Goodwill is not a cost of service line item. It is "built through high quality management and service."[460] WGL argues that "[R]atepayers do not have an equity stake in the utility, nor have they paid for the enhancement of the intangible assets, which have been built by the Company's management."[461] WGL concludes that "[I]ndirect attempts to acquire or dilute the ownership of utilities should be summarily dismissed."[462] Furthermore, WGL says utility affiliates should be permitted to use the utility's name/logo "since affiliates of other large corporations with whom they compete will have this same advantage in the marketplace."[463] WGL also claims that there has been no evidence to show that affiliate use of a utility name or logo is a barrier to the

[457] *Id*.
[458] Docket No. 55, Appendix A at 6.
[459] Docket No. 80 at 6.
[460] *Id*.
[461] *Id*. at 7.

[462] *Id*.
[463] Docket No. 101 at 4.

development of competitive markets. It cites experience in its natural gas customer choice program to support this position.[464] WGL supports the current disclaimer requirement which it says avoids customer confusion regarding the utility-affiliate relationship. However, WGL "would object to the use of multiple disclaimers that will produce unnecessary confusion."[465] WGL would support the suggestion that all suppliers disclose the non-regulated nature of their product or service, "thereby maintaining the 'level-playing field' that should be available to all suppliers."[466]

Columbia says that "[N]o specific disclaimers are necessary, absent a showing that the utility and its affiliate have engaged in promotional activities or communications that are misleading or deceptive."[467] Columbia says a ban on affiliate use of a utility name/logo is unfair to consumers because some consumers may prefer to take service from a utility affiliate.[468] Columbia says "consumers are clearly entitled to know just who they are dealing with."[469] Columbia claims that requiring affiliates to adopt a dissimilar name "would almost certainly lead to complaints that consumers had been tricked into dealing with utility affiliates."[470] Columbia emphasizes that there is no legal basis for a prohibition, particularly where the marketing affiliate is a separate entity not subject to the utility's control. Columbia and the marketing affiliate are separate subsidiaries of Columbia Energy Group. Further, "the Columbia name and logo are not assets of Columbia, and the Company has no authority to dictate what names or logos can be used by other affiliates within the Columbia Energy Group."[471]

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[464] *Id*. at 4-5.
[465] *Id*. at 6.
[466] *Id*.
[467] Docket No. 49 at 5.
[468] Docket No. 98 at 4.
[469] *Id*. at 5.
[470] *Id*.
[471] *Id*.

The Joint Commenters take the position that "consumers and competition would best be served by an outright ban on affiliates' use of the utility's brand name and logo."[472] Alternatively, they support imposition of a royalty for use of the utility's brand name and logo.[473] The Joint Commenters say that use of a similar brand name or logo by an affiliate "is one of the most effective means by which a utility can transfer its incumbency advantages to its unregulated affiliates."[474] They also say:

> Even with the strictest disclaimer requirements, there is bound to be some customer confusion about the relationship between a similarly named affiliate and the utility that has been providing that customer's service for years. Indeed, regardless of corporate intent, a similarity of business names between the affiliate and the utility will tend to create the false impression that the affiliate has all of the attributes of the regulated utility merely by virtue of its corporate affiliation.[475]

The Joint Commenters say that a royalty would compensate ratepayers for the use of these valuable assets and offset an affiliate's advantage over competitors. Discussing royalties in Case No. 8577, the Commission said that a company "ought not price valuable services or assets to subsidiaries at levels that it would be unwilling to give, under the same terms and conditions, to a third party."[476] The Joint Commenters conclude that "imposition of a royalty payment for the use of the utility's brand name and/or logo is therefore fully consistent with the principle upon which Case No. 8577 turned."[477] However, if affiliates are permitted to use the utility trade name or logo, then the Joint Commenters recommend the following disclaimers be required for all communications regarding the affiliate:

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472 Docket No. 61 at 14.
473 *Id*.
474 *Id*. at 13.
475 *Id*.
476 *Id*. at 14 quoting Case No. 8577 at 37 (86 Md. PSC 239).
477 *Id*.

- the affiliate "is not the same company as [*e.g.*, BGE], the utility";
- the affiliate is not regulated by the Maryland Public Service Commission; and
- "you do not have to buy [the affiliate's] products in order to continue to receive quality regulated services from the utility."[478]

However, they say that the disclaimers should be limited to the use of the name/logo in Maryland. Lastly, the Joint Commenters say that the Commission should retain the requirement that affiliates may not represent that an advantage accrues in the use of utility services as a result of dealing with the affiliate.[479]

The Joint Commenters note that the Commission has stated that utilities and their affiliates are to be treated as separate entities.[480] Consequently, "the law of trademarks provides guidance on how the Commission should treat 'separate entities' with the same or similar names."[481] The Joint Commenters argue that trademark law provides a 13 part test to determine whether a likelihood of confusion exists under the Lanham Act § 2(d).[482] Factors include: similarity of marks, similarity of the goods, similarity of trade channels, sophistication of the party, fame of the prior mark, and the number of sellers who use the mark.[483] The Joint Commenters conclude that the Commission should "find that the use of similar names by the utility and its affiliates is likely to lead to customer confusion."[484] Further, Dr. Gordon's suggestion that an affiliate shares the utility's history of service, would "be highly misleading" according to the Joint Commenters.[485] Dr. Gordon also suggests that an affiliate's use of a utility's name or logo will improve

[478] *Id*. at 23.
[479] *Id*.
[480] Docket No. 84 at 5.
[481] *Id*. at 6.
[482] *Id*., See Application of E.I. DuPont de Nemours & Co., 476 F. 2d 1357, 1360-62 (C.C.P.A. 1973).
[483] *Id*. at 6-7, citations omitted.
[484] *Id*. at 8.
[485] *Id*.

“accountability.” However, the Joint Commenters say that as a result of separation, the utility will not be accountable for anything that the affiliate does. “The accountability stops at the affiliate, unless the utility is violating other standards of conduct regarding separation.”[486] The Joint Commenters also claim that “the entry barrier associated with the utility’s name and logo recognition would deter potential competitors from entering the market.”[487] They also say that a simple ban will involve less day-to-day monitoring than any attempt to enforce fair use of the utility’s name or logo.[488] While the Joint Commenters support a ban, at least in the utility’s service territory, they say that the ban need not be in perpetuity. Perhaps three years will be sufficient to permit competition to begin to take root.[489] The Joint Commenters also say that “the utilities’ trade names and logos have acquired secondary meanings over the decades that they held state-granted monopolies.”[490] “Thus, the names and logos should be protected from appropriation by ‘separate entities’, such as the affiliates.”[491] As for disclaimers, the Joint Commenters say that “lack of an extensive disclaimer would restrict the amount of information available to the customer, forcing the customer to make ‘poorly informed choices’”.[492] Furthermore, the complaint process is inadequate. It “deals with the problem in a post hoc fashion.”[493] Also, “the complaint procedure takes too long to resolve issues.”[494]

The Joint Commenters say that BGE HOME has failed to establish a separate brand identity for itself, but rather has increased customer confusion. Further, BGE

[486] *Id*. at 9.
[487] *Id*.
[488] *Id*. at 10.
[489] *Id*.
[490] *Id*. at 21.
[491] *Id*.
[492] *Id*. at 29.
[493] *Id*. at 30.
[494] *Id*. at 31.

HOME's use of the BGE name will confuse customers regardless of any disclaimers.[495] The Joint Commenters cite claims of actual customer confusion to support their recommendation of a ban.[496] The Joint Commenters argue that "caveat emptor is not the appropriate standard by which to judge the confusing effect of utility and affiliate behavior."[497] The Joint Commenters also argue that BGE should be prohibited from including BGE HOME's number on its automated customer service telephone message because this would allow both of them to take advantage of confusion which they initiated.[498] "By creating this consumer confusion, BGE and Home have also created an excuse to engage in joint marketing and promotion of their goods."[499] This should not be permitted, the Joint Commenters say. The Joint Commenters also say that BGE HOME has exacerbated the confusion through continuing use of BGE identifying marks on its vehicle fleet.[500] The Joint Commenters say, "[T]his confusing combination of names, logos, phone numbers, and colors remains on Home's vehicles even five years after the company's incorporation. Only after photographs taken by the Alliance were introduced in this case did Home identify four vehicles that still had the BGE logo on them and take steps to remove the logo from the offending vehicles."[501] This "violated the code of conduct prohibition on joint promotions."[502] Further, "the vehicles reinforced the public's perception that BGE and Home are the same entity."[503] The Joint Commenters also say that BGE HOME's claim that it adopted its name to create a distinctive brand is undermined by the actions of Conectiv. Delmarva decided to pursue a new brand identity

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[495] *Id*.
[496] *Id*. at 19-21.
[497] *Id*. at 21.
[498] *Id*.
[499] *Id*. at 22.
[500] *Id*. at 23.
[501] *Id*.
[502] *Id*. at 24.
[503] *Id*.

and consequently, chose "a completely new name as an umbrella for all of its companies."[504] Therefore, "to establish its new identity, Delmarva distanced itself from its old name, ensuring that consumers would not automatically associate the new brand identity with the regulated company."[505] The Joint Commenters note that BGE's parent has also adopted a new umbrella name, Constellation, which is used by all but two subsidiaries. The Joint Commenters argue that the motivation for not changing BGE HOME's name is the same as BGE's, "to take advantage of the 183-year value of the name."[506] The Joint Commenters conclude, "[S]ignificantly, the one BGE affiliate that uses a version of the utility's name is the affiliate that is marketing to the consumers most likely to be confused by use of a similar name—residential consumers."[507]

The Joint Commenters argue that if an affiliate wants customers to know its relationship to the parent, then "[T]he Commission could permit the affiliate to include a statement with its name indicating that the affiliate is a subsidiary of the parent company. For example, BGE Home, under a name other than BGE, could state that it is a subsidiary of Constellation Enterprises, Inc."[508] The Joint Commenters say that because "customers of an affiliate are not actually dealing with the utility or its employees, [and] any attempt to convince them of a meaningful linkage between the affiliate and the utility is deceptive."[509]

The Joint Commenters also respond to the constitutional arguments proffered by the utilities.[510] According to the Joint Commenters, "[A]lthough commercial speech

[504] *Id*. at 27.
[505] *Id*.
[506] *Id*. at 28.
[507] *Id*.
[508] *Id*. at 29.
[509] *Id*. at 28.
[510] *Id*. at p.31-36.

receives some protection under the First Amendment, it merits only a type of intermediate scrutiny."[511] They note that Central Hudson applies a four-part analysis.[512] First, misleading or unlawful speech is not protected. Therefore, "[t]he government may ban forms of communication more likely to deceive the public than to inform it."[513] If the speech passes the first *Central Hudson* test, then the government must satisfy three additional tests to validly regulate the commercial speech. The regulation must be based upon a substantial state interest, it must directly advance this interest, and the regulation must be narrowly drawn to meet the state interest.[514] The Joint Commenters argue that "the first prong of this test is dispositive because the affiliate's use of the utility's name is misleading or deceptive."[515] According to the Joint Commenters, the U.S. Supreme Court ruled in *Friedman v. Rogers* that trade names qualify as commercial speech because they acquire a secondary meaning that the public associates with an expected level of quality or price of goods and services.[516] The Joint Commenters conclude that "[I]n this case, the presentation of the affiliate's name in conjunction with the utility's name is deceptive because it does not contain completely accurate information about the 'separate entity' relationship between the affiliate and the utility."[517]

The Joint Commenters say that the Commission should only require disclaimers for affiliates of regulated utilities because the risk of confusion exists only because of similar names.[518] "Consumers do not automatically associate either non-affiliated companies or distinctly named affiliates with regulation, as they do with affiliates using

[511] Docket No. 84 at 31. *See Florida Bar v. Went For It, Inc*., 115 S. Ct. 2371, 2377 (1995).
[512] *Id*. at 32.
[513] Docket No. 84 at 32. See *Friedman v. Rogers*, 99 S. Ct. 887, 896-97 (1979); *Edenfield v. Fane*, 113 S. Ct. 1792, 1799.
[514] *Id*. at 32, paraphrasing *Central Hudson*.
[515] *Id*. at 33.
[516] Docket No. 107 at 33, citing *Friedman* at 895.
[517] *Id*. at 36.
[518] *Id*. at 36.

the utility name."[519] As an alternative to requiring non-affiliates to use a disclaimer, the Joint Commenters propose that licensing regulations prohibit companies from advertising or suggesting that their prices are regulated.[520] The Joint Commenters agree with utilities that there is an immense practical difficulty in incorporating a disclaimer in every situation in which an affiliate uses the utility name. Therefore, a ban is the best solution to this problem.[521]

The Joint Commenters continue to argue for imposing a royalty when an affiliate uses a utility's name/logo. It says that "[T]he real question is whether the name and logo are utility assets."[522] The Joint Commenters argue that an affiliate's use of the Conectiv name is "a transfer of value from the parent entity," "similar to the source of value in the Constellation name."[523] In contrast, use of the BGE name by BGE HOME "is an unambiguous transfer of value" from BGE, the utility.[524] "To avoid cross-subsidy, BGE should not permitted to transfer this valuable asset to an unregulated affiliate without appropriate compensation."[525] As for measuring the amount of the royalty, the Joint Commenters say this can be done "using analyses from experts and economists."[526]

Summarizing the position of the Joint Commenters, they say that an affiliate's use of the utility name/logo creates two special problems. First, potential customers of the affiliate may be deceived into assuming that there is a relationship between services of the utility and the affiliate that does not, and under the code of conduct cannot, exist. Second, utility ratepayers may cross-subsidize the affiliate because the utility makes valuable assets, its name, logo and therefore reputation, available without charge to the

[519] *Id*. at 37.
[520] *Id*. at 37-38.
[521] *Id*. at 38.
[522] *Id*. at 39.
[523] *Id*.
[524] *Id*.
[525] *Id*.

affiliate.[527] The Joint Commenters conclude, that in the absence of an outright ban "strict disclosure requirements and the imposition of a royalty payment" are "the best means for addressing the deception and cross-subsidy issues inherent in use of similar names by utilities and their affiliates."[528]

Enron/Statoil is a strong proponent of disclaimers. They recommend that the existing code of conduct be modified to include the following disclaimers:

- Neither a utility nor its affiliates shall imply or express that their affiliation allows the affiliate to provide a service superior to that available from other suppliers.
- Neither a utility nor its affiliates may directly or by implication represent that the MPSC regulated services provided by the utility are of a superior quality when energy or energy-related services are purchased from a utility affiliate.
- Whenever a utility affiliate provides written mass marketing materials to the public using the utility's name or logo, it shall include a disclaimer that states that (i) the affiliate and the utility are not the same company, (ii) the affiliate is not regulated by the MPSC, and (iii) the customer does not have to purchase the affiliate's products in order to receive regulated service from the utility.
- In the case of electric utilities, neither an electric utility nor its affiliates may directly or by implication represent: (i) that merchant service (power sales) provided by an affiliate is being provided by the utility; (ii) that the power purchased from a supplier that is not a utility affiliate may not be reliably delivered; and (iii) that power must be purchased from a utility affiliate to receive the utility's MPSC regulated services.
- In the case of gas utilities, neither a gas utility nor its affiliates may directly or by implication represent: (i) that merchant service (gas commodity sales) provided by an affiliate is being provided by the utility; (ii) that the gas purchased from a supplier that is not a utility affiliate may not be reliably delivered; and (iii) that gas must be purchase from a utility's affiliate to receive the utility's MPSC regulated services.
- In the case of combined gas and electric utilities, neither a utility nor its affiliates may directly or by implication represent: (i) that merchant service (gas commodity sales and/or power sales) provided by an affiliate is being provided by the utility; (ii) that the gas and/or power purchased from a supplier that is not a utility affiliate may not be reliably delivered; and (iii) that gas and/or power must be purchased from a utility's affiliate to receive the utility's MPSC regulated services.[529]

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[526] *Id*. at 40.
[527] Docket No. 107 at 18.
[528] *Id*.
[529] Docket No. 60 at 14.

Enron/Statoil says that use of "utility names themselves provides a competitive advantage to affiliates who use them."[530] It also provides affiliates with a head start on the playing field."[531] Further, Enron/Statoil contends that "[c]ompetitive goals are served only if utility affiliates are made to market and attract customers based on the quality and price of their own stand-alone services, and not on the strength and name recognition of the utility."[532] Enron/Statoil says if common use of names/logos is not prohibited, then affiliates must be required to "pay fair market value for such use" and disclaimers must be imposed "to educate consumers and protect against misleading representations."[533] Summarizing, Enron/Statoil proposes the following affiliate disclaimer: "(i) the affiliate and the utility are not the same company, (ii) the affiliate is not regulated by MPSC, and (iii) the customer does not have to purchase the affiliate's products in order to receive regulated service from the utility."[534] In addition, neither the utility nor its affiliates should be allowed to imply or express that their affiliation allows either entity to provide superior service."[535] "In fact, the disclaimers proposed by Enron and Statoil Energy are identical to those proposed by OPC, Alliance and Maryland Natural Gas."[536] Enron/Statoil says that "[C]onfusion and manipulation are real threats to non-residential customers also."[537] Therefore, they recommend that the Commission "make its disclaimer requirement broad enough to capture all mass marketing materials, without regard to customer class."[538]

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[530] *Id*. at 15.
[531] *Id*.
[532] *Id*.
[533] *Id*. at 16.
[534] *Id*. at 28.
[535] *Id*.
[536] *Id*., Maryland Natural Gas is referred to as the Joint Commenters in this Order.
[537] Docket No. 104 at 9.
[538] *Id*.

MAPSA says that at a minimum, the Commission should require a conspicuous disclaimer that: "(a) the affiliate and the utility are different companies; (b) the affiliate's prices and services are not regulated by the Public Service Commission; (c) that the affiliate's services are of no greater quality than that of unaffiliated companies; and (d) that the price and reliability of utility services are in no way contingent upon obtaining the services of the affiliate."[539] MAPSA also says Dr. Gordon's disclaimer recommendation is "weak and ineffective."[540] "Merely declaring that the utility and its similarly or identically named affiliate are not the same company fails to inform the customer of the ramifications of engaging in business with the affiliate should the customer choose to do so."[541] In addition, merely adding the word "unregulated" to the simple disclaimer will confuse matters even more.[542] In particular, "suppliers of electric generation, whether or not affiliated with a utility, will be subject to some form of regulation."[543] According to MAPSA, "[J]oint marketing, affiliate use of a like or similar name or logo, and under-regulated utility-sponsored customer education efforts all promote market confusion and thwart competition."[544] Further, "[C]ustomers and competition may be irrevocably harmed when regulators do not move promptly and decisively to address problems that arise within the framework of a competitive market."[545]

The Alliance "maintains that unregulated affiliates must not be permitted to use names or logos that are identical or similar to those of their affiliated utility."[546]

[539] Docket No. 63 at 5.
[540] Docket No. 86 at 10.
[541] *Id*.
[542] Docket No. 109 at 7.
[543] *Id*.
[544] Docket No. 63 at 11.
[545] *Id*. at 12.
[546] Docket No. 87 at 11.

However, if such use continues to be allowed, the Alliance recommends the following disclaimer:

> (1) that the affiliate is a separate corporation/entity from the utility;
> (2) that the affiliate's prices and terms of service are not regulated by the Maryland Public Service Commission;
> (3) that the relationship between the affiliate and utility does not mean that the quality of the affiliate's services are superior to that of similar services performed by unaffiliated companies; and
> (4) failing to conduct business with the affiliate will have no impact, positively or negatively, upon the provision of regulated services.[547]

The Alliance says that its recommended disclaimer "permits the affiliate to identify its relationship with the utility, but precludes a situation where that relationship might be used to obtain a competitive advantage or to otherwise deceive the customer.[548]

The Alliance has also addressed the legal authority of the Commission to prohibit affiliate use of utility names/logos.[549] The Alliance concludes that "[T]he Commission has the legal authority to preclude affiliates' use of the same or similar name and logo of their regulated utility affiliate."[550] The Alliance, concurring with the Joint Commenters, says that affiliate use of a utility's name does not pass the first prong of the *Central Hudson* test, that the commercial speech must concern lawful activity and not be misleading.[551] Further, the Court of Appeals has said the standard for deception is whether a material representation or omission has occurred that is likely to mislead consumers acting reasonably under the circumstances.[552] The Alliance says that it is important that The Consumer Protection Act does not require that a consumer actually be

[547] Docket No. 59 at 18.
[548] *Id*. at 19.
[549] Docket No. 108 at 11 to 34.
[550] *Id*. at 11.
[551] *Id*. at 15.

deceived.[553] The Alliance concludes that Maryland utilities have structured affiliate relationships "to deliberately create and capitalize upon the confusion created in the minds of consumers by the affiliates' use of the utilities' names."[554] The Alliance also emphasizes that the likelihood of confusion between affiliates and utilities has increased where affiliates move into specific product lines identical to that of the associated utility.[555] The Alliance also argues that its Exhibit 2 "adequately demonstrates that the likelihood of customer confusion is inescapable."[556] The Alliance concludes that "the Commission is absolutely justified, and in fact, obligated by its duty to serve the public interest, to preclude affiliates' use of regulated utility names."[557] The Alliance also argues that "the utility name and logo have substantial value to the unregulated affiliates."[558] Since cross-subsidization is prohibited, the Alliance says an alternative is to impose a royalty, although this is less desirable than an outright ban.[559] However, implementing a royalty "in no way" addresses the confusion caused by such usage.
"Thus, while there may have been a time when a royalty was appropriate, it now appears that the Commission is left solely with the option of simply precluding the affiliates' uses of the names."[560]

OPC says that an affiliate's use of a utility's name and logo "provides a significant advantage especially in dealing with residential customers, where the cost to reach and sign up new customers can be a large barrier."[561] "It is little wonder," OPC says, "that the Constellation Energy Group, parent of Baltimore Gas and Electric,

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[552] *Id*. at 16, citing *Luskin's Inc. v. Consumer Protection Division*, 353 Md. 335 (1999).
[553] *Id*. at 18.
[554] *Id*.
[555] *Id*. at 21-22.
[556] *Id*. at 25.
[557] *Id*. at 31.
[558] *Id*.
[559] *Id*.
[560] *Id*. at 34.

retained the ‘BGE’ name only for BGE Home Products & Services, which markets to residential customers.”[562] OPC argues that “[T]he impact of the utility’s name and logo is most significant in the utility’s own service territory, but virtually nil outside of its service boundaries.”[563] OPC says affiliate use of the utility brand “creates a form of cross subsidy” because the brand “implicitly confers information about product quality and is generally associated with goodwill”, thereby lowering costs and increasing sales versus competitors.[564] Additionally, it creates an entry barrier if the affiliate is not required to pay for the brand.[565] OPC concludes that the “power of the utility brand can be so great . . . as to effectively wipe out competition.”[566] OPC claims that such damage to competitors in a newly competitive market cannot be undone and that the market is permanently altered.[567] OPC also claims that “[N]o amount of customer education and disclaimers can undo the security that many

customers will associate with continuation with a name brand they recognize and have received reasonable service from over the years.”[568] According to OPC, “[D]etails of separate corporate relationships cannot be explained succinctly and effectively in disclaimers, especially by the utility and affiliate in whose interest it is to keep the barrier fuzzy.”[569] Summarizing, OPC says prohibiting affiliates from using the name and logo of the incumbent utility, at least in the utility’s service territory will avoid misleading or confusing customers, avoid creating price or efficiency distortions in the affiliate market, is a better solution than trying to mitigate problems with disclaimers and detailed

[561] Docket No. 50 at 4.
[562] *Id*.
[563] *Id*.
[564] *Id*.
[565] *Id*.
[566] *Id*.
[567] *Id*. at 5.
[568] *Id*.
[569] *Id*.

monitoring, and will allow appropriate development of new competitive energy markets.[570] OPC says that if affiliate use of the utility name/logo is permitted, it "could be compensated by a royalty to ratepayers of the utility."[571] OPC says that if name/logo usage is not banned, then "a disclaimer similar to the following . . . is recommended for all print and internet information presented by the affiliate:

> PG&E Energy Trading is not the same company as Pacific Gas & Electric Company, the utility, and is not regulated by the California Public Utilities Commission. Customers of Pacific Gas and Electric Company do not have to purchase products or services from PG&E Energy Trading to continue to receive quality service from Pacific Gas and Electric Company.[572]

"A shorter form approved by the Commission could be used in radio and television advertising."[573]

OPC says that a further disclaimer is required when promoting DSM services under a public benefits charge. It recommends the following:

> You do not have to purchase electricity from Baltimore Gas and Electric Company or its affiliated company(ies) [INSERT THE WORDS ABOUT AFFILIATES AND THE NAME OF ANY AFFILIATE(S) ACTIVE IN THE ENERGY MARKET HERE IF APPLICABLE, e.g., BGE Home Products and Services] to receive energy efficiency services. These services are offered to all residential customers, regardless of electric service provider, in the area where BGE provides distribution service.[574]

OPC says that a utility brand is "an intangible asset whose name recognition and quality reputation has been built at ratepayer expense."[575] OPC argues that this "is not a brand

[570] *Id*. at 6.
[571] *Id*.
[572] *Id*. at 30.
[573] *Id*.
[574] *Id*.
[575] Docket No. 77 at 1.

that has been developed through competitive efforts."[576] OPC claims that the "information the brand conveys . . . may not even be accurate or relevant."[577] This is because the utility's reputation, a result of a monopoly energy business, will not necessarily produce the same quality under different market conditions requiring different expertise.[578] OPC says it is "particularly concerned that consumers could be harmed if an affiliate is able to obtain an economic advantage (i.e., through name and logo) that allows it to capture a greater market share than it otherwise would have without providing real value in terms of price or service quality in exchange."[579] While OPC recommends full corporate separation and prohibition of the utility brand in the utility territory, it says less stringent requirements are applicable outside the utility's service area. OPC says that the "primary distinction between levels of applicable codes of conduct should be based on the scope of the utility's brand recognition, not the energy-related and non-energy-related distinction from Case No. 8747."[580] OPC also makes the argument that adding the utility affiliate to the newly competitive market may, in fact, not be good for competition. This is because competitors could be driven out of the market by confused consumers who "choose the affiliated company that is 'supposed' to provide the service because (in the view of the confused customer faced with name and logo) the same company has always done so in the past as the integrated utility."[581] OPC also claims that affiliate use of the utility name/logo aggravates customer inertia to create an unequal playing field.

OPC says that when affiliates use the utility brand, they are "attempting to send a message to consumers that there is some benefit to the affiliate in the competitive market

[576] *Id*.
[577] *Id*. at 2.
[578] *Id*.
[579] *Id*.
[580] *Id*. at 4.
[581] *Id*. at 5.

by being connected to the utility."[582] This is contrary to the Commission's position. "Even under the loose separation rules of Case No. 8747, the Commission has attempted to ensure that the affiliates maintain a separate operation from the utility."[583] According to OPC, the record in this case "contains persuasive evidence that there exists a substantial confusion among the public as to offerings being made by utility affiliates."[584] OPC says that because utility services will remain a regulated monopoly, its need for advertising is extremely limited and the benefits of the use of the same name all accrue to the affiliate. Therefore, OPC concludes that there is not really any economy of scope.[585] OPC noted that the utilities have responded to the branding issue "by stating that ratepayers have not gained an interest in Company property . . . by years of paying for regulated service."[586] However, OPC says that this argument "is contrary to the argument made by utilities for stranded cost recovery."[587] OPC noted that "the utilities had no qualms with ratepayers having an interest in generating plants which utilities believe to be a liability."[588] OPC concludes that if ratepayers are responsible for a liability, they should have an interest in property that has accumulated a net benefit during the regulatory period.[589] OPC claims that it "is the ability of the Commission to carry out the regulatory task assigned to it by the Legislature which is responsible for the price, service quality, and reliability of utility service that customers associate with the incumbent utilities."[590] OPC also claims that the disclaimer required by Case No. 8747, simply that the affiliate is an affiliate of the utility, "probably does more to emphasize the

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[582] Docket No. 103 at 24.
[583] *Id*. at 25.
[584] *Id*. at 26.
[585] *Id*.
[586] *Id*. at 30.
[587] *Id*.
[588] *Id*.
[589] *Id*. at 30-31.
[590] *Id*. at 31.

connection between the utility and the affiliate to the benefit of the affiliate than it does to clarify the situation for the average consumer."[591] OPC goes on to say that it "is not opposed to a requirement that all suppliers in the market, for at least some transition period, be required to identify for consumers that the price of their product is not regulated by the Public Service Commission."[592] OPC also says that the branding "prohibition can be reviewed after a transition period to determine if the restriction can be removed without misleading consumers."[593]

OPC also argues that the Commission has the legal authority to prohibit an affiliate from using the utility's name or logo. OPC's argument emphasizes the Commission's traditional authority over utilities. OPC claims that the record in this case supports a finding that such usage "results in the misleading of customers, impedes the creation of a competitive market, and results in cross-subsidization of the affiliate by utility ratepayers."[594] OPC argues that the Commission "has the authority under its basic ratemaking function to issue an Order which dictates the conduct necessary by utilities and its affiliates to prevent cross-subsidization."[595] OPC argues that "if the Commission has the authority to prohibit the utility from claiming a benefit based on its affiliation with the utility and had the authority to prohibit the affiliate from occupying the same business location as the utility, it has the authority to prohibit use of the utility name and logo of the utility if the Commission finds, as a matter of fact, that such action is necessary to prevent subsidization of the affiliate by utility ratepayers."[596] OPC also said that the Legislature has envisioned a transition period during which the Commission

[591] *Id*. at 33.
[592] *Id*. at 34.
[593] *Id*. at 35.
[594] *Id*. at 35.
[595] *Id*.
[596] *Id*. at 36.

would act to ameliorate the risks to consumers and the competitive market of a transition from regulated to competitive services. OPC says these risks arise "because consumers will not have the knowledge necessary for the functioning of a truly competitive market at the beginning of retail competition in electricity supply and electricity supply services, there remains a regulated alternative to the services being offered on a competitive basis, and consumers are apt to be confused or misled by the state's change in regulatory policy."[597]

The AG-CPD stated that "[T]he electricity marketplace must allow consumers to make informed purchasing decisions. This will allow competition to be based upon product, service, and price, as it should be."[598] In addition, consumers need "complete and accurate information regarding the goods and services" utilities and others are offering.[599] Initially, the AG-CPD took the position that "consumers need to know who is making the offer and the relationship of that entity to other companies participating in the electricity marketplace."[600] In its Reply Comments, the AG-CPD stated that "[U]pon reflection, however, we realize that no amount of disclosure can overcome the misimpression given to consumers by an affiliate's use of its parent utility's name or logo in its advertising and promotional materials."[601] Since regulated utilities will operate separately from affiliates, "the utility's reputation for reliability, experience and quality of service has no relevance to the operation of the affiliate."[602] When an affiliate uses the utility brand "it does so to create the impression that its relationship with the parent utility is a relevant fact for consumers to consider when selecting a gas or electric supplier."[603]

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[597] *Id*. at 39.
[598] Docket No. 52 at 1.
[599] *Id*.
[600] *Id*.
[601] Docket No. 71 at 1.
[602] *Id*.
[603] *Id*. at 1-2.

AG-CPD concludes that if the relationship is not relevant, then it is "misleading to consumers to refer to it in advertising and promotional materials."[604] The AG-CPD urges the Commission to prohibit utility affiliates from using the utility name or logo, "or other reference to the parent utility in advertising, marketing and promotional materials."[605] "Such a prohibition would be consistent with the Consumer Protection Act's general prohibition against false and misleading oral and written statements that have the capacity, tendency or effect of deceiving or misleading consumers."[606]

Staff noted that in Case No. 8747, the Commission reaffirmed its decision in Case No. 8709 that an affiliate that uses a utility's name or logo must prominently display a disclaimer that the utility and the affiliate are separate entities. "Staff recommends that this disclaimer be adopted in this case as well."[607] Staff noted that the utilities generally resist any further disclaimers. The utilities say that the name and logo are corporate property and that restrictions generally violate First Amendment free speech rights. The marketers and OPC advocate substantial additional disclaimers which they say are necessary to avoid customer confusion. Staff says that the intent of these extra disclaimers is already covered by Staff's recommended standards of conduct. However, Staff did revise its position in its Reply Comments.[608] In addition to the Case No. 8747 disclaimer, that the utility and affiliate are separate entities, Staff recommends "a more comprehensive disclaimer for electric company affiliates."[609] Staff argues that "[I]nherent in a utility's name is [the] impression that the entity's prices are subject to review and verification by the Commission."[610] Consequently, Staff recommends that an

[604] *Id*. at 2.
[605] *Id*.
[606] *Id*.
[607] Docket No. 51 at 23.
[608] Docket No. 73 at 13-14.
[609] *Id*. at 13.
[610] *Id*.

affiliate that uses a utility brand display an additional disclaimer "indicating that the affiliate's prices are not regulated by the PSC."[611] In its Post-Hearing Comments, Staff noted that it has again "re-analyzed" this issue and presented a further "modified proposal."[612] Staff noted its concern with possible consumer confusion and "the natural implication [is] that the two entities are or may be the same and as such that the Commission regulates the affiliate."[613] "The inclusion of a disclaimer acknowledging an affiliate relationship does little to dispel the misconception," Staff says.[614] Therefore, "Staff recommends that the Commission require the affiliate to use a variety of disclaimers."[615] "The choice of disclaimer would be dependent upon the activity the affiliate is engaged in."[616] Staff says that the "basic disclaimer," that the Commission does not regulate the affiliate's prices and services will serve as a "flag" to the consumer. "Staff further recommends that this disclaimer be required of all marketers/suppliers, so that there is minimal confusion regarding the Commission's role in the commodity market."[617] Staff also says that requiring this "unobtrusive disclaimer" of marketers assists the Commission in fulfilling its responsibilities under the Act.[618] Staff says "[T]he intermediate disclaimer would restate that the Commission does not regulate the affiliate's prices and services, and that the affiliate is not the same company as the utility. The most stringent disclaimer would add that the consumer does not have to purchase the affiliate's services in order to receive regulated services from the utility."[619]

[611] *Id*.
[612] Docket No. 105 at 7-9.
[613] *Id*. at 7.
[614] *Id*. at 8.
[615] *Id*.
[616] *Id*., See Appendix 2.
[617] *Id*.
[618] *Id*.
[619] *Id*.

Staff also addressed the constitutional issues.[620] Staff says that the U.S. Supreme Court has made it clear that commercial speech receives "a limited measure of protection, commensurate with its subordinate position in the scale of First Amendment values, while allowing modes of regulation that might be impermissible in the realm of noncommercial expression."[621] Further, the Supreme Court has "recognized the validity of reasonable time, place, or manner regulations that serve a significant governmental interest and leave ample alternative channels for communications."[622] Staff says trade names convey information based upon association. Staff argues that "when the association implied is misleading, ambiguous or is contrary to a legitimate state interest, the use of that trade name, without qualification, is objectionable."[623] Staff noted that the "Supreme Court has held that restrictions on the use of trade names are permissible where the State has a substantial and demonstrated interest in protecting the public from deceptive and misleading information, and where factual informational advertising may be communicated freely and explicitly to the public."[624] Accordingly, there is no First Amendment rule . . . requiring a state to allow deceptive or misleading commercial speech whenever the publication of additional information can clarify or offset the effect of the spurious communication."[625] Staff proposes that affiliates that use the utility name/logo "provide a disclaimer which clarifies the relationship of the utility and the affiliate and the jurisdiction of the Commission."[626]

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[620] *Id*. at 22-27.
[621] *Id*. at 23, citing *Ohralik v. Ohio State Bar Association*, 436 U.S. 447, 456 (1978).
[622] *Id.* at 24, *citing Consolidated Edison Company of New York v. Public Service Commission of New York*, 447 U.S. 530, 535 (1980).
[623] *Id*. at 26.
[624] *Id*., citing *Friedman v. Rogers*, 440 U.S. 1, 15-16 (1979).
[625] *Id*. at 26-27, citing *Friedman* at 13, n.11.

2. Commission Decision

(a) Royalties – Name/Logo and other Intangible and Unquantified Benefits

The Commission determines herein that it will not require an outright ban on the use of a utility's brand name and logo by an affiliate. However, the Commission finds that use of a utility's name or logo by an affiliate constitutes a transfer of a valuable asset from the utility to that affiliate. It is also clear that this valuable intangible asset is difficult to quantify, but valuable nonetheless, because of the power of the brand in the market and the related quality, reputation and accountability suggestions that are conveyed to consumers. Further, the Commission adopts the position of many of the parties that the transfer of the name and logo requires that some compensation is due to the utilities, and indirectly the ratepayers, for the affiliate's use of the assets, which value was built at ratepayers' expense. Not only does the name/logo have value that must be recognized, but the "transfer" of this asset to an affiliate is anti-competitive because no other company would be permitted to use the asset without compensating the utility. Therefore, the Commission adopts, in principle, the concept of a royalty.

In addition, the Commission will apply this concept to other intangible or unquantified benefits, services, or assets being transferred from a regulated entity to growing numbers of affiliates. These decisions support an earlier decision herein, which finds the existing definition of utility asset to be too narrow and expands that definition to include intangible assets and unquantified assets.

Both OPC and the marketers supported outright bans on the use of brand name and logo. OPC proffered that development of a market could be harmed by affiliates, and the use of name and logo may allow an affiliate to capture a greater market share than it

[626] *Id*. at 27.

would otherwise if customer decisions were based solely on price and value. Some marketers stated that use of the name and logo may create market power problems. However, the marketers and OPC agreed that if the Commission did not impose an outright ban on the use of the brand name or logo as they advocated, then the Commission should at least impose a royalty to allow the ratepayers to have some benefits accrue to them. Marketers also said that imposing a royalty on utilities would compensate ratepayers for the use of intangible assets and offset an affiliate's advantage over its competitors in the marketplace. The marketers and OPC argued that the transfer of all utility assets must be compensated.

The utilities take the position that requiring an affiliate to pay a royalty would be an unreasonable policy because it has no basis in economics. Further, they say that the name and logo are utility assets that have never been included in the rate base. Therefore they claim that ratepayers are not entitled to anything because this asset has never provided the company revenue through the rate of return. They say that goodwill and other intangibles have been accumulated through good management and service. Utilities also claim that the reason marketers want them to pay a royalty is to increase affiliates' cost of doing business so that they can undercut an affiliate's price.

In Order No. 74038, in Case No. 8747, the Commission determined that "a utility's affiliates may use the utility's name or logo but neither the utility nor its affiliates may represent that any advantage will accrue to customers or others in the use of utility services as a result of that customer or others dealing with the affiliate."[627] That decision represented a continuation of a Commission policy from Case No. 8709 wherein the

[627]Case No. 8747, Order No. 74038, 89 MD. PSC 54, 89 (1998).

Commission permitted BNG, a gas marketing affiliate, to be identified as an affiliate of BGE.[628]

The Commission has carefully reviewed the extensive record on this matter in this case and finds that it is inappropriate, at this time, to modify the decision in Case No. 8747 and require a ban on affiliate use of a utility's name or logo. Therefore, the Commission declines to prohibit a utility affiliate from using the brand name and logo of the regulated entity.

The Commission is persuaded that, at this point in the restructuring process, it is appropriate to continue to permit affiliates to use the name and logo of their associated utility, but under the guidelines provided in this Order. The Commission notes its concern with this practice. The Commission credits the concerns raised by OPC, AG-CPD and the marketers regarding the use of name and logo. However, the Commission declines to require a ban on this practice. Instead, the Commission will permit an affiliate to use the utility name and logo, but will require the utility to impute royalty revenues for transferring this valuable intangible asset. Alternatively a utility may forego the opportunity to permit an affiliate to use its name and logo and thereby avoid the imputation of a royalty. In addition a royalty will provide just and reasonable compensation to the utility for use of its assets.

The Commission has determined previously that affiliates of a regulated utility must be considered as stand-alone, separate entities. The decision to impute a royalty under certain circumstances does not undermine this determination. This Commission has a long history of making decisions to achieve just and reasonable rates which reflect its best efforts to apply appropriate cost allocation methodologies. Iimposition of a

[628] Case No. 8709, Order No. 72523, 87 MD. PSC 43, (1996).

royalty is designed to accomplish this objective. It is just another tool that the Commission now adopts to preclude utilities from subsidizing affiliate activities.

The royalty concept is not new. The use of a royalty to recognize the inherent value of certain transfers of utility property was first discussed at length in Case No. 8577.[629] In that proceeding, the Commission focused upon transfers of intangible assets, such as the name and logo, as well as transfers of unquantified benefits to an affiliate of BGE. Several parties, including Staff and OPC, advocated imputing a royalty to the regulated utility based on gross revenues of the affiliate. This payment sought to capture the intangible or unquantified benefits which the affiliate receives from a utility in addition to capturing some of the value related to the use of the name and logo. BGE argued that intangible assets are shareholders' property and that a royalty would result in an unwarranted subsidy to the utility, which does not correspond to any expense.

The Hearing Examiner concluded in Case No. 8577 that it was appropriate to impute a two percent royalty to the utility to compensate BGE for intangible benefits provided to its affiliate as well as for other unquantified benefits which exist when there is not strict structural separation between the two entities. His finding was based, in part, upon Staff's testimony concerning royalties imposed by other state commissions, citing in particular a case involving Rochester Telephone Company.[630]

The Hearing Examiner also affirmed, and the Commission later upheld, a corollary issue determined in Case No. 8487. In that case, the Commission required BGE to reflect operations of BGE's unregulated Gas Appliance and Service Department above-the-line because of the substantial intertwining of both entities. Over time, the

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[629] Case No. 8577, Order No. 72107, 86 MD. PSC 225, (1995).
[630] *Re Rochester Telephone Company*, 145 PUR 4th 419; *aff'd,* Re Rochester Telephone Company v. PSC of New York, 614 N.Y.S. 2d 454 (N.Y. App. Div. 1994); *aff'd,* Re Rochester Telephone Company v. PSC of New York, 87 N.Y. 2d 17, 660 N.E. 2d 1112 (1995).

imputation of shared costs and revenues continues as substantial benefits and cross-subsidies continue to flow to what has now become BGE Home. This imputation of revenues to the utility is a part of the just and reasonable determination process and results in more reasonable rates for the ratepayers. The most recent Commission decision upholding this practice occurred on June 19, 2000 in Case No. 8829.

In Case No. 8577, Staff argued that a royalty is consistent with fully distributed cost allocation principles. Staff asserted that BGE's approach to cost allocation resulted in ratepayers paying rates which exceed the cost of service, in part, because it overlooks intangible and unquantified benefits. However, according to Staff, a royalty operates to correctly allocate all costs and expenses so that an accurate cost of service is established. By establishing an accurate cost of service, a royalty is helpful in aiding the Commission in implementing just and reasonable rates as required by law.[631] In addition, Staff argued that there was an expense associated with developing the name and logo and that cost is reflected totally in utility rates. The royalty allocates some of the cost to the affiliate. Staff asserted that the Hearing Examiner's Proposed Order did not confer any property rights to ratepayers in the corporate name or logo. The purpose of a royalty, Staff said, is to allocate costs to the affiliate for the use of intangible assets and for use of shared services that would be uncompensated in a fully distributed costing method. In addition, Staff opined that a royalty reflects the inherent unreliability of allocations; it captures misallocations that are difficult to detect, quantify and prove. Finally, Staff argued that a royalty provides an administratively efficient way to avoid piecemeal allocations.

[631] See Section 4-102(b) of the PSC Law.

In Case No. 8577, OPC also supported imposition of a royalty and agreed with Staff that the Commission's reasonable rate standard cannot be fulfilled if BGE is permitted to allow affiliates to use corporate assets without just compensation. OPC concluded that there is value associated with intangible assets which is not accounted for in BGE's cost allocation process. OPC emphasized that no firm would allow another unrelated entity to use its name and logo without appropriate compensation. OPC maintained that just because tangible costs might be properly allocated through a fully distributed cost methodology does not mean that intangible benefits are allocated properly. OPC suggested that the Hearing Examiner chose to capture many of the unquantifiable benefits in the royalty imputation instead of fine tuning BGE's current cost allocation procedure. OPC concluded that a royalty is an administratively cleaner, less costly form of regulation. OPC also asserted that an imputed royalty should reflect favorably on the utility's financial condition with the financial community. The royalty could be quantified by appraisers at an appropriate time. OPC argued that imputation of a royalty results in fair and reasonable compensation for the intangible and unquantifiable benefits provided to the affiliate when there is not clear structural separation between the two entities. OPC concluded that imposition of a royalty is an appropriate regulatory response for the relationship that exists between BGE and the subsidiary.

BGE, of course, took a much different position. BGE contended that the fully distributed cost allocation procedures reflects all costs that should be charged to the affiliate and protects ratepayers from cross-subsidization. According to the Company, since all costs are fully allocated, there are no benefits left to deal with and therefore, there is no rational basis for the royalty. BGE argued that ratepayers do not have a property right in a utility's name and reputation. It claimed that any value associated with its reputation is a result of BGE's management and the dedication of its employees. BGE also disputed the Hearing Examiner's finding that BGE's name has value because it is a monopoly. Since competitors would not pay a royalty, BGE concluded that unilateral application of a royalty would be an anti-competitive penalty. BGE also noted that in the *Rochester Telephone Company* case, the New York Commission imposed a royalty on total capitalization, not on gross revenue. BGE asserted that a royalty based on gross revenues has no relationship to the benefits the subsidiary receives. BGE also criticized implementation of a royalty because it claimed that it sends the wrong signal to the financial community. According to BGE, a royalty would limit BGE's ability to compete, thereby eroding confidence in the financial community and create negative implications on the cost of capital.

In Case No. 8577, the Hearing Examiner found that based upon that record, it was fair and reasonable to impute a royalty payment in the amount of two percent upon the gross revenues of the nonutility operations as compensation for the intangible benefits and unquantified benefits provided by BGE to its affiliate in situations where there is not clear structural separation between the two entities[632]. The Hearing Examiner stated that, "[T]he record is clear that BGE provides benefits to the subsidiary which the subsidiary gets from its affiliation to the Company, and I find that it is a reasonable ratemaking practice to impute some measure of these benefits back to the parent company as a fair recognition of the benefits the subsidiary enjoys through its affiliate relationship."[633] The Hearing Examiner emphasized that "a royalty also recognizes the fact that the Company itself admits there are certain services that the Company believes are too small or too

[632] Case No. 8577, Order No. 72523, 87 MD PSC 225, 258 (1995).
[633] Id.

difficult to reasonably quantify which are provided to the subsidiary."[634] The Hearing Examiner concluded that "a royalty provides some compensation to the utility to balance the incentives for affiliated companies to shift costs to the regulated operations."[635] The Hearing Examiner also stated that "as all parties recognize…there is clear value to the intangible benefits of the corporate name and logo, which assets can clearly be marketed to the public and outside enterprises, and I find a royalty payment is the proper method to fairly recognize the use of such corporate assets."[636] "Clearly, the corporate reputation is an asset which has been greatly contributed to by the parent company's status as a regulated utility, and ratepayers have contributed to the value of the corporate reputation by their payments of rates over the years and their status as a large, captive customer base of the utility with an ongoing customer relationship."[637]

In Order No. 72107, issued August 4, 1995, the Commission chose not to adopt the royalty proposed by the Hearing Examiner in Case No. 8577. The Commission stated that it preferred to more completely examine BGE's current cost allocations on an issue by issue basis using the allocation principles adopted therein to ensure that utility operations do not subsidize the affiliate. The Commission also stated: "The underlying principle for these kinds of imputations is the fact that the Company ought not price valuable services or assets to subsidiaries at levels that it would be unwilling to give, under the same terms and conditions, to a third party."[638] Sales of goods and services to affiliates at below market prices raise legitimate issues regarding fairness, the Commission declared. Therefore, the Commission decided that it would make

[634] Id.
[635] Id.
[636] Id.
[637] Id.
[638] Id. at 239.

accounting adjustments based on market pricing principles for services, and on asymmetrical pricing principles for assets.[639]

The Commission finds that it is an inescapable fact that the name, logo, reputation, and goodwill of a utility constitute very valuable intangible utility assets.[640] Equally clear is the fact that the use of name and logo by an affiliate constitutes a transfer of these valuable assets, along with reputation and goodwill. Utilities have argued that since these assets are not included in rate base, the ratepayers are not entitled to any compensation for such asset transfers. However, their argument fails to recognize that utility name and logo are utility property. As OPC said, it is important to remember that the utility position here is contrary to that which they adopted in their stranded cost cases. There the utilities argued that ratepayers had an interest in generating plants that the utilities' claimed were liabilities. OPC argues it is only fair that the ratepayers have an interest in intangible assets that have increased in value during the same regulatory period.

The Commission agrees. Based upon the record in this proceeding, the Commission concludes that it is inappropriate to permit utility companies to transfer valuable intangible property to another legal, stand-alone entity without just and reasonable compensation to the utility. The Commission is charged by law with ensuring that rates are just and reasonable and that a utility's financial integrity is maintained. Failure to provide for an imputation of revenue to a utility when it is shown to be

[639] Id.

[640] For example, Pepco argued that "a rule prohibiting utilities and their affiliates from using the same logo and trade name would constitute a taking of utility property under the Fifth and Fourteenth Amendments which would necessitate the payment of just compensation." Docket No. 106 at 15. Obviously, this argument is based on the assumption that the name and logo have significant value that could be determined in an evidentiary proceeding.

appropriate would result in rates that are higher for ratepayers, than would be appropriate under the just and reasonable standard.

The record is clear in this proceeding that affiliates have not compensated their associated utility for the use of their name and logo. Consequently, the Commission has concluded that, in principle, a royalty will provide an appropriate mechanism to rectify this practice to some extent. Further as Staff noted in Case No. 8577, a royalty is compatible with the fully distributed cost allocation methodology used for transfers of tangible assets and shared services.

In Case No. 8577, the Commission did not uphold the Hearing Examiner's application of a royalty to intangible or unquantified transfers but rather to focus on appropriate allocation of costs for transfers of tangible goods and assets. However, in this Order, the Commission accepts the argument proferred by many of the parties in this proceeding that the previous definition of utility asset was too narrow and did not fully reflect the various benefits and cross-subsidies that can flow from the regulated entity to an affiliate.

The record is clear that utilities should be appropriately reimbursed for all assets transferred to affiliates. Processes were adopted in the past including the four pricing principles, CAMs in one case and verification procedures for others to assure that appropriate accounting occurred for asset transfers from regulated entities to their affiliates. Despite those efforts in prior cases, it appears that certain costs have been transferred between the regulated and unregulated entities, which have not been accounted for or have been accounted for in an incomplete method. Even with the use of a CAM, certain costs remain unquantified and there is no assurance that ratepayers are not providing a subsidy. *De minimus* amounts are not included despite the cumulative effect, book values may be used as opposed to market value despite escalation in value over time, and the value of having a guaranteed source of revenue through the regulated entity is not reflected. For example, when a utility guarantees a debt incurred by an unregulated affiliate, loans an affiliate money, or carries unreconciled debts, risks are imposed on the financial well-being of the utility with potential repercussions for ratepayers. Many such unaccounted for values are highlighted in the comments of Staff and other parties in this proceeding.

Therefore, the Commission finds that it is appropriate, in principle, to impute a royalty to the regulated gas and electric utilities, with the exception of municipal utilities, in this State: (1) For the value of the name and logo of a gas or electric company used by an affiliate in the State; and (2) intangibles, unquantified assets or *de minimus* benefits conferred on affiliates because of a lack of complete separation between the regulated and non-regulated entities. The utility is not entitled to give away assets, no matter the recipient. A royalty captures the value of assets such as those listed above.

This decision builds on prior decisions of the Commission in Case Nos. 8487, 8577, 8697, and 8829. The Commission found and repeatedly affirmed that the value of benefits and services accruing first to BGE's Gas Appliance and Service Division, and subsequently to BGE Home, was so intertwined with the regulated service that a sharing of revenues was appropriate, despite being separate entities. In this instance, upon imposition of a royalty, the Commission will consider the elimination of that sharing provision.

The Commission will docket two separate proceedings. One will determine the appropriate value to be imputed to the utility for use of the utility's name and logo. The second will determine the appropriate value for unquantified and other intangible benefits transferred that should be imputed to a utility. Each gas and electric utility as well as Staff, OPC, and other interested parties will have a opportunity to address these issues in a proceeding designed to sharply focus and resolve each of the two royalty issues.

(b) Disclaimers

In Case No. 8747, the Commission determined that if an affiliate uses the utility's name or logo, then a prominent disclaimer that the utility and affiliate are separate entities must be displayed by the affiliate. As expected, the utilities have generally advocated that no new disclaimers be required. However, in their post-hearing comments, some utilities and affiliates supported additional disclaimers under certain circumstances. The utilities have also suggested that if affiliates are required to display a disclaimer, then in certain instances marketers should be required to do likewise.

The marketers generally supported a ban on an affiliate's use of a utility name or logo. In the alternative, they have recommended requiring a number of disclaimers. The marketers emphasized that disclaimers are required to educate customers, provide them with necessary information and minimize customer confusion. They also recommended that disclaimers be broad enough to capture all mass marketing materials, without regard to customer class. OPC, the Alliance and the Joint Commenters supported Enron/Statoil's disclaimers or similar standards. However, the marketers resisted the application of any disclaimers to themselves. The marketers did agree with the utilities that there is an immense practical difficulty in incorporating a disclaimer for every situation where the affiliate uses the utility name or logo. The marketers also stated that it is appropriate to limit the use of disclaimers to affiliate activity in Maryland.

OPC argued that an affiliate that uses the utility's name or logo has a significant advantage in dealing with customers in the utility's own service territory, particularly in dealing with residential customers. OPC also argued that a specific disclaimer is required when DSM services are promoted under a public benefits charge. Staff proposed a variety of disclaimers, which would depend upon the activity in which the affiliate is engaged.

The Commission doubts that extensive disclaimers will be of significant value to consumers. Consumers may not be attuned to subtle distinctions in energy regulation. Therefore the Commission has adopted concise disclaimers, written in plain english that provide useful information to consumers. If a core service affiliates identifies itself as an affiliate of a utility, or uses the name or logo of an associated utility, then it must prominently display a disclaimer in all mass marketing or advertising that states:

> The (name of affiliate) is not the same company as the (name of regulated utility) and prices and services of (name of affiliate) are not set by the Public Service Commission.

If a non-core service affiliate identifies itself as an affiliate of a utility or uses the name or logo of an associated utility, then it must prominently display a disclaimer in all mass marketing or advertising that states:

> The (name of affiliate) is not the same company as the (name of regulated utility).

I. Enforcement and Penalty Provisions[641]

1. Parties' Positions

The utilities generally take the position that the Commission's current powers, particularly its complaint procedures, are sufficient to enforce its rulings. Dr. Gordon

[641] This section addresses Issue No. 17 – What enforcement and penalty provisions should be developed by the Commission for violations relating to the Standards of Conduct?

testified that, "[P]enalties and enforcement expenditures should be proportionate to the costs and risks to consumers from violations of the Commission's standards."[642] In other words, "they should be based on economics," and "should not be so draconian as to eliminate efficiencies arising from affiliate competition."[643] Further, any penalties for rules violations "should be based on the likely social costs of infractions."[644] The size of the penalty should reflect the harm done to consumers and the cost of enforcement. Dr. Gordon says the standards of conduct should establish the framework for addressing violations. "Specific issues can then be addressed on a case by case basis," he concludes.[645]

Conectiv says that "the Commission's complaint procedure is available to resolve disputes."[646] The Commission can issue cease and desist orders and craft appropriate reporting requirements to deal with violations. Conectiv argues that "penalties should be imposed only in particularly egregious cases."[647] It says penalties are not appropriate for technical or inadvertent violations.[648] While the Commission should take note of its enforcement powers, Conectiv says particular violations are more appropriately resolved on a case by case basis.[649] Pepco concludes that there "is no need for special enforcement and penalty provisions" because the Commission "already has sufficient mechanisms in place."[650] WGL, NUI and Columbia all support this position.[651] However, Columbia says that if new penalties are developed, they should be sufficient enough to deter violations but not so tough as to deter affiliates from participating in the

[642] Docket No. 56 at 23.
[643] *Id*.
[644] *Id*.
[645] *Id*.
[646] Docket No. 53 at 34.
[647] *Id*.
[648] *Id*. at 35.
[649] *Id*.
[650] Docket No. 64, Attachment A at 6.

market.[652] Chesapeake says serious complaints should be handled through the current complaint process on a case by case basis.[653] It argues that penalties "should be reserved for repeated or flagrant violations."[654]

The marketers support structural separation to prevent violations from occurring. They also recommend stiff financial penalties and emphasize the need for expedited complaint procedures. MAPSA says that the "magnitude of compliance and enforcement provisions is directly proportional to the extent of the interaction among utilities and affiliates."[655] "Further, the procedural approaches that have worked well in the past, relative to a regulated industry must be revisited in parallel with the development of utility standards of conduct in order to ensure that the Commission is able to address anti-competitive infractions on an expedited basis.[656] The PGA recommends that complaints be filed in writing with the utility or affiliate and that responses to the complainant be filed within 45 days.[657] If the complaint cannot be resolved informally, then the complainant may file a complaint with the Commission or seek any other relief permitted by law.[658]

The Joint Commenters say that the Commission "should adopt efficient, low cost, timely enforcement procedures and should match penalty provisions to the nature and magnitude of the violations."[659] They recommend that all utility affiliate intercharges be public to aid in the detection of violations. Enforcement mechanisms should also

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[651] Docket No. 55, Appendix A at 6, Docket No.69 at 12 and Docket No. 49 at 6.
[652] Docket No. 49 at 6.
[653] Docket No. 54.
[654] *Id*.
[655] Docket No. 63 at 5.
[656] *Id*. at 12.
[657] Docket No. 45 at 6.
[658] *Id*.
[659] Docket No. 61 at 27.

"facilitate the intervention by affected consumers and competitors."[660] The Joint Commenters also argue that any utility found violating the code of conduct should be required to reimburse all reasonable costs of the complainant.[661] They conclude that, "[I]f the selected punishment appropriately fits the crime, the Commission may succeed in deterring similar anti-competitive behavior by other utilities."[662]

The Alliance says that "appropriate penalties should be modeled upon other penalty provisions contained in the Act."[663] The Alliance argues that code of conduct penalties should be modeled upon the penalty provisions for electric supplier violations which are contained in §7-507(l) of the Act; a civil penalty of not more than $10,000 per violation. The Alliance concludes that, "[T]here is no reason to suggest that utilities and affiliates who violate code of conduct provisions should face less severe penalties for infractions than competitive suppliers of electricity."[664]

Enron/Statoil emphasizes that monitoring by the Commission and Staff is essential.[665] Enron/Statoil says the Commission should make it clear that if the rules are violated the Commission may terminate the inappropriate transaction or prospectively restrict the amount, percentage or value of transactions between the utility and its affiliates.[666] Penalties should not be recovered from utility ratepayers according to Enron/Statoil.[667] However, penalties should not preclude injured persons from seeking

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660 *Id*.
661 *Id*. at 28.
662 *Id*.
663 Docket No. 59 at 21.
664 *Id*. at 22.
665 Docket No. 60 at 26.
666 *Id*.
667 *Id*.

damages in court.[668] Local distribution companies should be required to notify ratepayers of violations.[669]

OPC argued that penalties for violation of affiliate transaction regulations should be large enough to dissuade the utility from considering them a 'cost of business.'"[670] Penalties should range from $5,000 to $20,000 per violation. In addition, penalties should reflect the injury to ratepayers and competitors and the seriousness of the violation.[671] Repeated violations should result in more severe sanctions. Under certain circumstances, the Commission should prohibit utility/affiliate interactions for an appropriate period due to violations.[672] However, none of OPC's recommendations should preclude exercise of any of the Commission's existing enforcement powers.[673] Finally, OPC suggests that, "[T]o the extent legally feasible, all collected fines could be deposited in a fund that would support the Commission's complaint resolution process."[674]

MEA addressed the issue of suspension of electricity supplier licenses. It stated that "the issue of suspension of licenses is closely linked to the other issues involved in affiliated transactions, and demands comment."[675] MEA noted that the Act authorizes the Commission to suspend or revoke electricity supplier licenses.[676] MEA argues that the severity of this sanction demands that the Commission not delegate this authority to a utility.[677] MEA asserts that it would be unsound regulatory policy to expect a utility to fairly determine suspension or revocation issues regarding a non-affiliated supplier's

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668 *Id*.
669 *Id*.
670 Docket No. 50 at 34
671 *Id*.
672 *Id*.
673 *Id*.
674 *Id*. at 35.
675 Docket No. 72 at 3.
676 Id. §§7-507(k)(l) and (n).

license at its sole discretion, or even with Commission review on an after-the-fact basis.[678] "MEA believes the Act reserves revocation and suspension authority to the Commission."[679] Consequently, MEA concludes that "Any revocation or suspension of a license should require a Commission Order."[680]

Staff recommends adoption of extensive complaint and penalty procedures.[681] Staff noted that §7-505 of the Act requires the Commission to adopt "policies and practices to prevent discrimination against customers, self-dealing, and undue or unreasonable preferences in favor of the electric company's own electricity supply, other services, divisions, or affiliates."[682] To address the need for timely resolution of code of conduct complaints, Staff recommends that the Commission modify its complaint procedures with respect to informational, service, and filing requirements, as well as the time period for answers and the structure of the review process.[683] "Staff stresses that these recommended modifications should only be applicable to complaints alleging violations of the gas and electric Standards of Conduct."[684] Staff suggests that complaints include information about the alleged action or inaction of the respondent which is the source of the complaint, including any financial impacts; a statement concerning whether the issues are pending in another case; the remedy requested; and any basis for preliminary relief.[685] Staff recommends equal specificity for the answer.[686] Staff says that service should be concurrently on the Commission and the respondent and

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[677] Docket No. 72 at 3.
[678] *Id*.
[679] *Id*.
[680] *Id*.
[681] Docket No. 51 at 25-31.
[682] *Id*. at 25.
[683] *Id*. at 27.
[684] *Id*.
[685] *Id*. at 29.
[686] *Id*. at 28-29.

in an expeditious manner.[687] Staff suggests that answers be filed within 20 days after the complaint is filed, unless the Commission indicates otherwise.[688] Staff also recommends that complaints be delegated to the Hearing Examiner Division on an expedited basis and that requests for preliminary relief be determined within 30 days.[689] In extreme cases, a "fast track" procedure should be established.[690] Again, Staff emphasizes that time is of the essence in these matters.[691]

Staff also noted that §13-201 of the PSC Law provides authority to fine a public service company that is in violation of any Commission rule, regulation, order, or law.[692] This section establishes a maximum penalty of $2,500 for each offense.[693] "Staff recommends that the Commission strictly enforce compliance and penalize violations to the fullest extent possible" because of the effect violations could have on the emerging competitive markets.[694] Staff argues that the penalty recommendations of some parties do not comply with the current state of the law.[695] Staff suggests that penalties be determined on a case by case basis because this will allow the Commission to retain the necessary flexibility to ensure that the penalty fits the circumstances of the offense.[696] Finally, Staff asserts that the "combination of active (reports and penalties) and reactive (complaint procedures) policies along with timely resolution of disputes should assist in making a smooth transition to competition."[697]

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687 *Id*. at 29.
688 *Id*. at 29-30.
689 *Id*. at 30.
690 *Id*. at 30-31.
691 *Id*. at 31.
692 *Id*. at 26.
693 *Id*.
694 *Id*.
695 Docket No. 73 at 18.
696 *Id*.
697 Docket No. 51 at 31.

2. Commission Decision

The Commission has broad authority to enforce the PSC Law and Commission orders and to protect consumers and suppliers from discriminatory, unfair, deceptive and anticompetitive acts and practices in the marketing, selling and distribution of gas and electric services. The PSC Law, including § 7-507(1) of the Act and § 7-603(a) of the Gas Act, authorize the Commission to levy fines of up to $10,000 per violation, revoke or suspend supplier licenses, order refunds and credits to customers, or impose other remedies to redress violations of Commission orders and to adjudicate complaints.

Given the potential risks associated with anticompetitive behavior and the market share implications associated with such conduct between utilities and their affiliates, companies should consider carefully the emphasis the Commission places upon the standards adopted in this Order and should be aware that the Commission will not hesitate to impose severe penalties upon companies that violate the rules of conduct set forth herein. Accordingly, the companies are expected, at the earliest opportunity, to give explicit instructions and directives to their affiliates concerning the requirements of this Order.

The Commission also has a complaint process in place. Title 3 of the PSC Law establishes a comprehensive set of rules and procedures for complaints, presentation of evidence and appeals. As in the past, these procedures will be used to resolve all complaints, including complaints involving electric and gas suppliers. At this time, the Commission believes that this is an appropriate process for promptly addressing complaints involving affiliate transactions.

Moreover, the Commission has begun a review of its complaint and dispute resolution procedures in light of the emerging competitive energy markets. In Order No. 75949, the Commission established the Complaint Procedure Design Group ("CPDG") to recommend additional streamlined and expedited procedures to facilitate disputes filed by customers, utilities, suppliers and other interested parties. Pending further action by the Commission on that matter, however, the existing procedures set forth in the PSC Law and in the Code of Maryland Regulations shall apply. The Commission finds that these represent appropriate complaint and enforcement procedures at this time.

VI. ORDERED PARAGRAPHS

IT IS, THEREFORE, this 1st day of July, in the year Two Thousand, by the Public Service Commission of Maryland,

ORDERED: (1) That the standards of conduct for utilities which are set forth in the text of this Order are hereby adopted for all gas and electric companies subject to this Order;

(2) That the policies and standards adopted in Case No. 8747 shall continue in force to the extent that they are consistent with this Order. Inconsistent standards are hereby repealed;

(3) That except as provided herein, the GENCO Code of Conduct, adopted by the Commission in Order No. 75757, for the Baltimore Gas and Electric Company, is adopted as the generic GENCO Code of Conduct for all appropriate electric utilities and shall govern all transactions between electric companies and their generation affiliates;

(4) That during the residential price cap period adopted in Case No. 8797, relating to Allegheny Power Supply, APS shall abide by the GENCO Code of Conduct approved by the Commission in Order No. 76009;

(5) That the cost allocation principles which are set forth in the text of this Order are hereby adopted for all gas and electric utilities subject to this Order;

(6) That the employee sharing and loan and loan guarantee provisions set forth herein are adopted for all gas and electric utilities subject to this Order;

(7) That Cost Allocation Manuals shall be filed as required in the text of this Order;

(8) That the promotional practices regulations found at Title 20, Subtitle 40 of the Code of Maryland Regulations do not apply to affiliates of gas or electric utilities;

(9) That separate proceedinga shall be docketed to determine the appropriate value that should be imputed to gas and electric companies for the use of the company's name and logo and other intangible or unquantified benefits;

(10) That the complaint and dispute resolution procedures set forth in the text of this Order are hereby adopted.

Glenn F. Ivey

Claude M. Ligon

Catherine I. Riley

J. Joseph Curran, III
Commissioners

Commissioner Brogan concurs in part and dissents in part.

APPENDIX A

GENCO Code of Conduct

a) While it serves as SOS provider, a utility shall not be able to market or promote its SOS. However, this limitation shall not preclude a utility from providing unbiased information to customers that SOS is available and the terms thereof.

b) Until June 30, 2006, the GENCO must sell all the generation output of the assets transferred under its settlement, including energy, capacity and other products (excluding all output sold to the utility for SOS) into the wholesale market.

c) Until June 30, 2006, the GENCO shall be a separate subsidiary from the unregulated retail marketing affiliate and separate from utility.

d) With respect to sales or any other transfer to any of its affiliates for resale to "retail electric customers" as defined in Code Section 1-101 (AA) (including but not limited to the utility's unregulated retail marketing affiliate) in the utility distribution service territory until June 30, 2003, the GENCO shall not offer power or ancillary services incident to the delivery of power at prices and terms more favorable than those available to non-affiliated electric suppliers. Such information regarding the above sales or transfers of power and ancillary services by the GENCO to its affiliate shall be simultaneously posted with the execution of any agreement for the sale or transfer on a publicly available electronic bulleting board. This provision shall not apply to sales by the GENCO to the utility for SOS.

e) A utility shall not market or promote the competitive supply service.

IN THE MATTER OF THE INVESTIGATION INTO AFILIATED ACTIVITIES, PROMOTIONAL PRACTICES AND CODES OF CONDUCT OF REGULATED GAS AND ELECTRIC COMPANIES.	* * * *	BEFORE THE PUBLIC SERVICE COMMISSION OF MARYLAND CASE NO. 8820

DISSENTING OPINION OF
COMMISSIONER SUSANNE BROGAN

I concur with the determinations made by the Commission with regard to the need for modifications to the standards of conduct, the adoption of pricing principles and the broad parameters of the regulation of the relationship between utilities and their affiliates set forth in this Order. I respectfully disagree, however, with the majority Opinion regarding promotional practices and the imposition of royalties for the use of name, logo and other intangible or unquantified benefits.

Promotional Practices

In this Order the Commission determined that the promotional practices regulations ("PPR") should not apply to affiliates and should remain in effect for gas and electric utilities, subject to later revision or repeal. I favor immediate repeal of the promotional practices regulations and see no reason for further proceedings on this matter or for revising these regulations.

The record in this case is sufficient to determine that the PPRs should be repealed. The gas and electric industries have undertaken many changes since the inception of these regulations in the 1970's. The shifting paradigm of these energy industries renders the PPRs unsuitable. The standards of conduct that have evolved through Case Nos. 8709, 8577, 8747 and this Case No. 8820 establish sufficient safeguards to warrant repeal of the regulations. Additionally, I note and concur with the Standard Offer Service marketing prohibitions placed on electric companies by this Order. Finally, as the majority Opinion notes, there are already statutory prohibitions on some promotional practices set out in § 4-503(b) of the PSC Law. I would place no further restrictions and would undertake immediate repeal of the promotional practices regulations.

Royalties

The majority Opinion in this Case adopts the concept of a royalty to compensate the utility and its ratepayers for the affiliate's use of the name, logo, and other intangible and unquantified benefits, services and assets. The value of the royalty will be determined in two separate proceedings. This appears to be an attempt to protect ratepayers from cross-subsidization by imputing a value for the benefits that an affiliate gets from its relationship with the utility. I disagree.

While I find merit in the notion that the value of the utility's name and logo results from the utility's provision of franchised monopoly service, I am persuaded that for purposes of pricing asset transfers, a utility asset is tangible property that is included in rate base. In setting rates for public service companies, the Commission is required to set rates that are just and reasonable.[1] Inherent in this requirement is the notion that the rates will yield operating income to the utility that accounts for depreciation and provides a reasonable return on the fair value of the utility's property used and useful in providing service to the public.[2] In order to include an asset in rate base and therefore recover its costs through rates, the asset must be used to provide utility service. If a rate base asset is used by an affiliate, the affiliate must compensate the utility for such use. To do otherwise would result in the ratepayer subsidizing the operations of the affiliate. The

[1] Section 4-102 of the PSC Law
[2] Section 4-101 of the PSC Law

name and logo and other intangible assets of a utility are not currently considered used and useful in the provision of service. The ratepayer is not paying for that intangible asset through rates. Therefore, use of the asset by the affiliate is not a ratepayer subsidy.

I also disagree with using a royalty payment as a means of capturing the value of unquantified benefits received by the affiliate from the utility. The majority Opinion seems to rely on the notion that a royalty will compensate for the inherent unreliability of the cost allocation process. While I agree that the fully distributed costing method and cost allocation process may be imprecise at times, I am uncomfortable ascribing some percentage royalty as a means of valuing unidentified or unquantified assets, services or benefits. If the asset or service can be identified and a value placed on it, then the cost allocation process should do so.

Legitimate concerns are raised by the affiliate's use of the utility's name or logo. When an affiliate uses the name/logo of the utility, customers are likely to believe that the companies are one and the same or that the quality of service of the affiliate is somehow superior.[3] The use of disclaimers is a less intrusive solution to the problems or confusions that arise from name and logo use. Core Standard No. 3 and Non-Core Standard No. 3 established in this Case require disclaimers. The addition of this new language to those standards was intended to eliminate customer confusion. With these requirements in place, the imposition of a royalty on the use of the name or logo seems extreme.

A royalty, in this instance, imposes financial burdens on the affiliate that surely will result in competitive disadvantages. In restructuring the gas, electric and telephone industries in this State, the Commission traditionally has emphasized the importance of

[3] Arguably that is a violation of Core Standard No. 1 and Non-Core Standard No. 1.

adopting policies that promote competition, not any specific competitors. The adoption of the royalty concept seems to deviate from this. It is conceivable that competition could be harmed given the fact that a utility marketing affiliate may play an integral role in transitioning the electricity market towards retail choice. The marketing affiliate may provide customers with a level of comfort because of its utility affiliation. Therefore customers who would be hesitant to choose an unknown supplier may indeed switch from utility-provided SOS to the marketing affiliate. This initial acceptance of the notion of choosing an energy provider, however tentative, may ultimately lead to a more competitive market. These benefits are eradicated if the marketing affiliate must either change its name or pay a royalty to the utility and thereby increase its costs.

My final concern is an equitable one. In Case Nos. 8577 and 8747, the Commission determined that royalties would not be imposed on a shared name or logo. The utilities relied on that decision first made in 1995. At the time of those decisions, the gas market was undergoing major changes and electric restructuring was imminent. The utilities made corporate structure decisions based on those 8577 and 8747 determinations. It seems unfair and overly burdensome to adopt changes now that will have major impacts while achieving no additional safeguards as a result of such actions. The protections that come from royalties can come from less extreme measures such as disclaimers.

My colleagues have reached well-reasoned decisions on Core and Non-Core Codes of Conduct, GENCO Codes of Conduct, SOS marketing restrictions, principles of cost allocation, pricing policies and a broad scheme of regulation of utility/affiliate relationships. I disagree with the majority Opinion's conclusions on the treatment of the promotional practices regulations and the royalty as a concept for capturing the value of the affiliate's use of the name/logo and other intangible and unquantified benefits and dissent from those portions of the Opinion.

Susanne Brogan
Commissioner