FINAL REPORT:

UTILITY COMPETITION WITH SMALL BUSINESS

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Office of Advocacy
Small Business Administration

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1.0 INTRODUCTION

1.1 Purpose of the Report
In March, 1984, the Office of Advocacy of the Small Business Administration issued a report entitled "Utility Competition with Small Businesses: Recommendations for States on Utility Energy-Related Programs and the Commercial and Apartment Conservation Service Program." This report discussed the impact on competition between utilities and small businesses of energy-related utility programs, and specifically the Commercial and Apartment Conservation Service Program (CACS). Based on its conclusion that CACS and other utility service programs may pose a serious threat to the well-being of many small businesses involved in the energy services market, the report recommended ways to minimize or eliminate unfair or illegal utility competition.

In the Fall of 1985, the Office of Advocacy decided to take a further, and broader, look at the competition issue. The Office of Advocacy decided that it would be valuable for an independent contractor to examine in greater depth the reasons for utility interest in diversifying into non-regulated, and competitive, energy-related fields; the elements of utility subsidization of these non-regulated activities; the potential remedies that small businesses have to counter unfair or illegal competition; the scope of the cross-subsidy problem; and the effectiveness of specific actions taken by small businesses against utilities. The purpose of this report is, therefore, to address these five areas, including five key case studies of actual small business complaints against alleged unfair or illegal utility competition.

1.2 Summary of the Issues
Electric and gas utilities across the country have, in recent years, entered into a wide range of businesses outside their publicly regulated activities as producers and distributors of energy. For various financial and strategic reasons, utilities are diversifying into a host of different fields, some related to their traditional roles, such as fuel exploration, transportation, and development, and some unrelated to energy, such as real estate, computer software sales, and telecommunications. As a regulated monopoly, the rates for, and profits from, its primary products, gas and
electricity, are determined by public commissions, giving the utility both restrictions and advantages. When the utility moves into unregulated sectors of the economy, its status becomes less clear. The regulatory restrictions no longer apply, but many of the institutional advantages may remain intact.

Although in almost every new venture, diversification brings utilities into competition with independent businesses already operating in the field, certain areas have been of particular concern to small businesses. Public utilities now sell appliances, provide plumbing, heating and cooling equipment and service contracts, perform home improvements in the form of insulation work and sales of storm doors and windows, market and service solar and other conservation devices, perform energy audits and provide a variety of other products and services which can be broadly referred to as energy services. These products and services have historically been supplied almost exclusively by small business enterprises. These businesses include plumbing, heating, air conditioning, electrical and insulation contractors, retailers and wholesalers. Utility entry to the energy services market received additional impetus from the National Energy Conservation Policy Act (NECPA) and the subsequent Energy Security Act (ESA), which federally mandated utilities to provide low- or no-cost energy audits, to residential customers, under the Residential Conservation Service (RCS) programs, and to commercial and multi-family customers under the Commercial and Apartment Conservation Service (CACS) program. Utilities were restricted, in some cases, from selling and installing conservation measures to residential customers under RCS, but no such prohibitions were included in CACS. The costs of the RCS and CACS apartment audits above $15 were to be subsidized by ratepayers.

It should be noted that the utility industry protested the establishment of the RCS and CACS programs almost as loudly as the small businesses who could not support their expenses through a ratebase and thus were effectively crowded out of the audit business. However, utilities do have other reasons for pursuing energy services markets. The reasons cited most often include:

- Profit-making opportunities, to increase returns to shareholders, bring in new capital, and/or offset other costs;
- As a response to competition among energy suppliers (electricity,
gas, fuel oil), to help maintain a utility's market share;

- To make use of in-house staff, such as engineers and other technical staff;

- For electric utilities, as a load management tool, to maximize the return on generating capacity and reduce the need for costly new capacity;

- To foster community development and public relations; and

- As a response to a perceived scarcity of local independent contractors.

In general, utilities argue that if they use assets that are otherwise underutilized, or if their programs have a positive effect on energy conservation and/or load management, they are in effect lowering the costs of energy and providing a substantial benefit to ratepayers. Utilities also tend to downplay the effect on independent operators. For example, according to one Edison Electric Institute estimate, out of 200 investor-owned electric utilities nationwide, supplying 98 percent of the nation's electricity, only 13 have engaged in sales and leasing of appliances. In contrast, appliance sales and leasing on the part of gas utilities occurs more frequently.

The small business community strongly disagrees, and argues that the threat to small businesses posed by unfair utility competition substantially outweighs any economic benefits. In 1984, a survey by the American Supply Association identified 90 utilities with business activities in direct competition with private enterprises. In a survey conducted the same year, over 50 percent of the members of the National Association of Plumbing-Heating-Cooling Contractors (NAPHCC) said that they were being adversely affected by utility competition. National organizations representing contractors and suppliers have formed several groups to focus on the problem, and formal actions against utilities have been brought before public service commissions in a number of states.

The basic complaint registered by small businesses is that, by the very nature of utilities, their entry into unregulated fields creates conditions where private businesses are simply unable to compete -- not because the utilities provide superior products or services, but because the utility has fundamental advantages, through its status as a regulated monopoly.
Utilities are able to undercut prices, and benefit from other marketing and operational advantages, by cross-subsidizing, i.e., using their regulated ratebase to subsidize unregulated activities.

1.3 Organization of the Report

The report is organized into four general sections, in addition to the introduction. Section 2 discusses the various elements of the competition issue, including the nature of cross-subsidization, cross-subsidization's impact on small business, reasons for increased utility diversification, antitrust and FTC involvement, and current remedies. The third section is a general case analysis which studies the range of complaints and cases raised by small businesses against utilities. This is followed by section 4 which analyzes five key cases illustrating, in greater depth, the nature of the complaints and cases being brought before public utility commissions (PUCs) and the courts. This section examines the legal jurisdiction of the PUCs and the courts, discusses the nature of the complaint, examines the decisions reached, and discusses the damages awarded. Finally, section 5 presents the report's conclusions and recommendations.
2.0 DISCUSSION OF THE ISSUES

2.1 Nature of Cross-Subsidization

Cross-subsidization can result from the misallocation of direct or joint costs to a utility's regulated activities, i.e., power production and distribution, to subsidize non-regulated activities. Generally speaking, state regulatory commissions prohibit a utility from using its regulated revenues to support unregulated activities. Energy audits, conducted as a part of government-mandated conservation programs, such as RCS and CACS, are, however, one notable exception: the utility is authorized by law to use ratepayer money to subsidize audit performance, at no more than $15 in the case of RCS; an audit for which an independent contractor would have to charge around $100. A number of other forms of cross-subsidization exist, some of which represent a direct cost to rate-payers and some of which do not. Among the advantages that a utility can bring to a non-regulated subsidiary activity are:

- **Capitalization** - The utility may provide loans, loan guarantees or other financial subsidies to a new business activity.

- **Credit ratings** - A subsidiary business can benefit substantially by sharing the parent utility's (usually excellent) credit rating.

- **Administration and overhead** - Management, planning, accounting, legal assistance, research and development resources may be used to start up, and in some cases to operate, other lines of business. In addition, office space, equipment, vehicles, computer facilities or personnel of the utility may be available.

- **Name recognition** - Instant name recognition, as well as a utility's image and position in the community, can be a valuable asset to other activities.

- **Credit information** - From customer's bill payment records, the utility has a built-in source of credit information for use in other business activities.

- **Billing** - Postage, mailing and personnel costs are already being paid by ratepayers. Adding charges for other business activities to the bill produces very little additional expense.
Advertising - In many states, advertising costs can be passed on to ratepayers. While advertising directly connected with an unregulated activity may need to be charged to that activity, there are many opportunities for the utility to also include material with advertising promoting its regulated activities. The postage for bill stuffers is paid by ratepayers as part of their utility bill. In addition, utilities can pool advertising dollars with appliance manufacturers more easily than independent businesses, creating greater cooperative advertising opportunities.

Direct mail - With utility bills going out monthly and with immediate access to customers initiating or terminating service, utilities have some of the most up-to-date mailing lists available.

Market data - Utilities frequently have extensive market data on their customers that could be made readily available for marketing of unregulated business activities.

Selective referral and market allocation - With its access to information on consumer needs and requests, a utility could arbitrarily refer or not refer business to selected businesses, or to its own non-regulated businesses.

Economies of scale - With larger volume orders, the utility can circumvent usual distribution channels and buy direct from manufacturers with possible favorable pricing.

Consumer financing - The utility's large capital base gives it access to providing favorable financing, which in some cases can be added directly to the utility bill.

Consolidated tax returns - Certain advantages can be gained by utilities consolidating the financial data of unregulated activities for tax purposes.

Where utilities charge substantially less than independent contractors for comparable services, some form of cross-subsidization, as discussed above, can be reasonably suspected. However, the line between legal and illegal cross-subsidization has been difficult to draw. Generally, cross-subsidization is permissible where ratepayers are receiving a benefit from the cross-subsidy, or the cross-subsidy is specifically required by law. Although there are current federal and state laws and regulations addressing
the issue, problems persist, not only in defining which practices constitute violations, but with identifying appropriate jurisdictions, and with tracking and proving unfair or illegal practices. Further complicating the legal perspective, state commissions generally have wide latitude in determining rules -- and exceptions to those rules.

In general, NECPA prohibits utilities from themselves supplying or installing residential energy-conservation measures, but this rule has certain exceptions. Those utilities that, on the date of NECPA’s enactment, were already supplying or installing measures can continue to do so (giving them so-called "grandfather" status). Other utilities may be granted waivers of the prohibitions. In addition, all utilities may supply or install conservation measures at the request of customers through contracts with independent suppliers.

The NECPA also establishes accounting procedures to keep expenses attributable to utility operation in energy conservation markets separate from expenses for other utility activities, and requires utilities to keep their accounts of expenditures for auditing and arranging services separate from all other accounts. The law directs utilities to treat the costs of providing customers with information about energy-conservation techniques as expenses of utility operation and to charge them to all ratepayers.

NECPA also authorizes each state public utility commission (PUC) to specify the manner of recovery of the "general administrative costs" of carrying out energy conservation programs, auditing homes, and arranging for energy-conservation work or loans. The amount recovered directly from a residential customer for whom these activities are performed may not exceed the lesser of the actual cost or $15. Treatment of other costs is in the discretion of the state PUC. Thus, PUC’s have discretion to permit utilities to expense or ratebase the costs of virtually any of their conservation activities, including sales and installation programs that they conduct pursuant to grandfathered status or waivers or by contract upon customer request. The options of treating costs of providing insulation or other energy conservation measures as expenses or including such costs in the rate base raise the possibility that energy conservation activities may be subsidized by the ratepayer.

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The language of the NECPA and the Energy Security Act reflect Congress's intent that utilities' energy conservation ventures be supervised with an eye toward preserving competition, and several sections contain language directing state PUC's to "prevent unfair methods of competition and unfair or deceptive acts or practices."

2.2 Cross-subsidization's Impact on Small Business

While these statutes address utility competition, they do so only in the limited sphere within energy conservation or renewable energy. Most of the complaints aimed at utilities do not involve energy conservation or renewable energy, nor do they involve the specific measures covered by NECPA and ESA. Recently, the predominant complaint has concerned utilities engaged in, or proposing to engage in, the servicing of equipment at prices well below that of competing contractors. Thus, many of the most controversial utility ventures fall outside the purview of federal law, with the possible exception of Section 5 of the Federal Trade Commission Act.

Another significant problem with existing legislation is that many PUC's have rejected claims based on competitive harm, and have disclaimed jurisdiction to consider the effects of utility operations on competition in unregulated markets. There are at least two reasons for this position. First, there is no specific mention of competition in unregulated markets in PUC authorizing statutes. From this absence, and the monopoly status of utilities, PUC officials may have drawn the conclusion that they are unable to consider competition policy. Many PUC's have restricted themselves to considering the possible effects of diversification on ratepayers, and if ratepayers were sufficiently insulated from possible loss, the effects on competition were, at best, secondary. Second, until recent years, regulated businesses were generally thought to be exempt from antitrust laws under the "state action doctrine" (state-approved utility conduct was exempt from application of the Sherman Act). This doctrine has been modified by recent Supreme Court decisions, which have found that utility action in unregulated markets is presently subject to antitrust scrutiny unless the state has expressed a "clear preference" for the restraint of competition. In some cases, however, states have not yet fully adjusted to this modified doctrine.
(See section 2.4 for further discussion of the antitrust and FTC aspects of the competition issue.)

Although there is no consensus among PUC's as to whether they should formally address competition issues, those PUC's that have considered the issue of cross-subsidization have often disallowed the utility's request to rate-base or expense its activities in traditionally unregulated markets. In general, these PUCs base their decisions on the principle that ratepayers should only subsidize unregulated activities which benefit all ratepayers equally. Whether or not such decisions have included concern for competition in their rationales, the effect, when costs have been properly allocated, has been to keep utility involvement in unregulated activities from restraining competition in those markets. However, sole reliance on the principle that the utility's activities in unregulated markets must not discriminate among ratepayers may not always coincide with the furtherance of competition when energy-conservation markets are involved. NECPA does not alter state law concerning the jurisdiction of the PUC's. But the NECPA framework does suggest that it may be in order for PUC's to reconsider discretionary decisions not to weigh competition in unregulated markets as part of the public-interest analysis of utility rate requests, at least with respect to those PUC decisions that relate to NECPA's Residential Conservation Service.

The NARUC Ad Hoc Committee on Utility Diversification issued a report and recommendations for state regulators in October 1982. The report addresses the problems posed to the ratepayers by diversification, and the cross-subsidization problem, in particular. The committee recommends that PUCs determine, in advance, appropriate areas for utility diversification to avoid problems before they arise. The PUCs must assure, under state law, access to the books and records of nonregulated activities to help protect against illegal cross-subsidization. The report also recommends that the utilities bear the burden of showing that the diversification plan is in the public interest, i.e., that the potential negative aspects do not outweigh the potential benefits.

The position of the Federal Trade Commission (FTC) has in general reflected the complexities in determining whether cross-subsidization is illegal in a specific case. It has been pointed out, for example, that cross-subsidization, per se, is not necessarily objectionable from the
point of view of competition policy. For example, if a utility must maintain
a fleet of vehicles or a group of workers in order to carry out its utility
operations, the antitrust laws do not prohibit the utility from using those
trucks or workers in some other business during slack periods, provided that
the proper costs of using the equipment is charged to the unregulated
business. Although this practice may result in injury to competitors,
there would be no injury to competition unless these activities were combined
with other anti-competitive activities. In other words, there is no anti-trust
violation if the utility maintains the cross-subsidy advantage, as long as
the utility is not committing other anticompetitive acts [FTC,1982].

Only when a subsidy becomes a means to anticompetitive ends, such as
below-market cost pricing to drive competitors out of a market so that the
subsidized venture can subsequently raise its prices to monopoly levels,
has the FTC seen cross-subsidization to be clearly illegal. Such "predatory
pricing" and attempts to monopolize violate both the Sherman Act and the
Federal Trade Commission Act. The other element necessary to support a
finding of attempted monopoly is a dangerous probability of success. A
utility's enjoyment of a monopoly position in its regulated market might be
taken as evidence of dangerous probability of success once the utility has
gained a degree of actual market power in the unregulated market. Under a
more flexible approach, a court might conclude that a dangerous probability
of success exists even before a near-monopoly share is obtained.

Although the FTC is on record as noting that "sustained pricing below
costs, however defined, by a company with substantial market power raises
the possibility of predation," the technical elements of predatory pricing
have been difficult to establish in specific cases. [FTC, 1982] Energy
conservation markets typically have low entry barriers, so it could be
argued that, having driven out competitors, the predator presumably would
have to face their re-entry if it raised prices to monopoly levels. Thus,
federal antitrust laws generally will not apply to the cross-subsidization
problem (without the presence of other anticompetitive behavior), although
the FTC is empowered to take action against anti-competitive activities
under Section 5 of the Federal Trade Commission Act. (See Section 2.4 below.)

A case has recently been made for more aggressive FTC action in preventing
unfair utility competition, particularly on the basis of two key arguments:
Since the state must clearly articulate an intention to displace competition in the market under consideration in order for antitrust immunity to be extended to private party activities, and then must actively supervise the party's conduct in that market, it would appear unlikely that new unregulated enterprises of utilities are beyond the reach of federal antitrust statutes. There is no indication that statutes in any state call for displacement of competition in the market for appliance sales, service and installation, home improvements and other services now being offered by utilities.

Utilities can use the resources of their monopoly enterprises to subsidize the operations of their new businesses in two ways. First, the subsidy may allow the unregulated enterprise to sell, service or install its product at a price below the cost of its unsubsidized competitors. Second, electric and gas utilities sell, service and install appliances and heating and cooling equipment at very low prices in an effort to obtain the largest possible market for the type of energy that they provide. The competition with monopoly utilities in unregulated markets can result in the destruction of non-utility competitors who do not have outside support. Both of these possibilities fall under FTC jurisdiction to bar violations of the spirit as well as the letter of antitrust laws, and to stop incipient activities that would, when fully developed, violate antitrust statutes. In addition, precedents exist for the FTC to address unfair methods of competition that it finds offensive to public values beyond those in the antitrust laws, particularly where injury to competitors is established. (See sections 2.4 and 2.5.1 for a further analysis of the FTC's role.)

It has generally been agreed that the unregulated enterprise should be charged the fair market value of the services provided by the utility. Otherwise, the utility's ratepayers -- including the utility's new competitors -- are forced to subsidize the utility's diversification program. The tremendous size of a utility compared to its new non-utility enterprise creates problems for its competitors because subsidies that have no identifiable effect on ratepayers can make a tremendous difference in the unregulated market.

State regulators in general maintain that impermissible cross-subsidization is not tolerated in regulatory policies and practice, and that all reasonable efforts are made to detect and remedy improper cost allocations.
Often, though, the burden for locating, among thousands of transactions, illegal cross-subsidizations in utility practices falls on small businesses, who may be faced with prohibitively lengthy and expensive actions before PUC's with limited resources and, often, limited interest in pursuing claims against utilities.

One approach recently suggested is the development of generic accounting procedures and methods for separation of financial transactions between a utility and its affiliates. The Virginia Legislative Committee, a consortium of regulated utilities that provide electric or gas service in Virginia, has supported the development of such generic procedures. [Virginia Legislative Committee, 1983] A review of existing literature and a survey of state commissions indicated that, although the lack of such procedures had been noted as an impediment to regulation of utility diversification by the National Association of Regulatory Utility Commissioners, none had thus far been designed or implemented on a generic basis. The procedures developed by the Virginia Legislative Committee were designed with three basic goals in mind:

- To preclude subsidization of non-regulated businesses by utility ratepayers and preclude subsidization of ratepayers by non-regulated businesses.
- To minimize time of Virginia State Corporation Commission staff required to audit transactions of a regulated utility.
- To provide an allowable basis for prospective consistent treatment of transactions between regulated and unregulated activities for all Virginia jurisdictional electric and gas utilities.

The procedures could productively be adapted to meet similar goals on a more widespread basis.

It must be recognized that even when the non-utility business is required to pay a market-based charge for services and products provided by the utility, the unavailability of similar services and products at comparable terms and conditions to competing business may still have an adverse effect on competition in the marketplace. However, under existing laws, strict accounting and market-based charges to unregulated businesses, if possible on a more stream-lined generic basis, are perhaps a practicable approach to restoring some level of functional fairness to the energy services marketplace.
-- and by extension to other marketplaces adversely affected by utility diversification.

2.3 Utility Diversification

The increased interest among utilities in diversifying into non-regulated business areas, including energy conservation services, has caused the potential for cross-subsidization to rise in recent years. Although cross-subsidization may not occur in all, or even most, cases of utility diversification, its likelihood increases as diversification efforts spread. Contractors' concerns center, in part, on maintaining a separation of regulated and non-regulated activities. This separation becomes more complex as the utility becomes more diversified, particularly when it enters areas unrelated to energy. As discussed in the preceding sections, achieving this separation requires the establishment of careful accounting procedures to appropriately allocate costs between the regulated business and the non-regulated business. Separating the different management functions so that managers and executives are devoting sufficient time to running the regulated utility also becomes crucial. Increased diversification thus complicates the role of public utility commissions who are responsible for seeing that utilities continue to provide a secure source of energy for ratepayers and that the latter are protected from paying for any non-regulated investments for which they do not derive a direct benefit or for which the risks are unusually high.

The causes for this trend toward diversification continue to be investigated. It is apparent, however, that they differ from one utility to another, depending, in particular, on the utility's financial situation and the entrepreneurial temperament of its management. The following general reasons are most often given for why utilities choose to diversify:

- Utilities want to ensure future demand for their products and future energy sources;
- Utilities' earnings are falling and therefore they need to diversify in order to raise earnings and, consequently, the value of their common stock;
- Utilities have retained earnings available which they are trying to spend;

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• Economies of scale may mean that utilities can provide services more efficiently than unregulated competitors;
• By diversifying, utilities will be able to attract and hold managerial talent; and
• Federal, state, and local programs may be encouraging utilities to diversify.

Each of these areas is discussed below in greater detail. A later section, analyzing complaints of unfair utility competition, will examine the role that these different motivations for diversification play in unfair competition complaints.

2.3.1 Ensuring Stable Energy Demand and Energy Sources

Utility diversification is by no means a new phenomenon. For many years, both gas and electric utilities have encouraged the sale and installation of appliances, which utilize their respective energy sources, through direct utility sales or through subsidiaries. These activities, which were generally carried out on a small scale, ensured the utilities of a demand for their energy output. Utilities have also owned subsidiaries such as coal mines, pipelines and drilling companies to ensure the availability of fuel and gas supplies.

Lower or stagnant energy demand and some leveling of prices between gas and electricity has played a role in increasing competition over end-use markets in recent years. This competition has sparked new fuel-switching efforts to encourage customers to change from electricity to gas, and vice versa. Fuel-switching efforts, which involve the sale and installation of appliances, lighting, and heating/cooling equipment, are frequently conducted through utility subsidiaries.

The motivation to diversify for purposes of securing a market for a utility's output has important ramifications for small businesses. For example, the utility may establish subsidiaries that will compete with existing independent businesses in selling and installing appliances; unfortunately, the utility may have an incentive to subsidize its sales and services with ratepayer funds. The incentive to sell or service appliances at or below cost exists because the higher demand this creates for gas or electrical appliances translates directly into higher demand for electricity.
or gas. The utility may believe that the increased demand for its particular energy source will more than offset the loss it takes on appliance sales and service. Clearly, a small business will have difficulty competing with a utility that chooses to pursue this course.

It should be noted that this same increase in demand for a utility's gas or electricity can be accomplished simply by utility subsidization of the sale of appliances or other products by independent businesses. This approach, which is taken by many utilities, can be as effective, yet does not pose a threat to competition.

2.3.2 Reduced Earnings

In addition to competition among different energy suppliers, one of the primary motivations for diversification appears to be a steady drop, or at least stagnation, in the earnings of many utilities. Malko [1981], for example, states that electric utilities' inability to earn their allowed rate of return is prompting their interest in diversification. In the case of gas utilities, according to a report published by the National Association of Regulatory Utility Commissioners (NARUC, 1982), their markets are not growing sufficiently to:

- support steady earnings growth...
- Earnings growth may become increasingly dependent upon higher prices for each unit of gas sold. [p.34]

This drop in earnings may be due to a number of factors, including higher capital costs, recent high inflation, and regulatory decisions that have not allowed utilities to recoup all the costs of recent construction projects, particularly for nuclear plants. Recently, however, many electric utilities are reporting substantial earnings increases.

The drop in utility earnings is seen as a serious matter by utility executives because common stock prices will fall, thus making capital more difficult to raise. Diversification is considered to be a solution for this drop in earnings in two ways. First, the utility can invest in businesses which have a higher earnings potential than electricity generation or gas distribution. This investment will raise earnings for the utility company as a whole, and thus attract more investors. Second, by diversifying, a utility may be able to reduce its risk profile, i.e., the variability of its earnings. Fluctuations in earning could be reduced if the businesses in
which the utility invests have counter-cyclical swings in their performance compared to the utility's energy production activities. If energy earnings fall but earnings from other activities rise, then the utility's overall earnings will remain relatively stable. This stability in earnings is regarded as a plus by many investors, who will thus pay a higher price for the utility's stock.

A corollary to the problem of lower earnings is the increase in certain utility costs, particularly for new generating capacity. The MARUC report points out that:

As electric utilities are or tend to become increasing cost industries ... the utilities may have a profit incentive to promote end use devices that reduce electricity consumption. [p.25].

In other words, utilities that are currently nearing the limits of their generating capacity now face major costs for expanding that capacity. These costs are due, in part, to more stringent safety and environmental regulations that have been instituted in recent years. A cheaper alternative to expanding capacity is to reduce demand through load management and conservation. Some of the primary methods for achieving these objectives are through the sale and installation of energy efficient appliances, the provision of audit services, conservation retrofit installations, and load-shifting.

The potential impact on small businesses of utilities diversifying, either to increase earnings or reduce costs, can be as significant as that resulting from fuel-switching efforts. Instead of an incentive to cross-subsidize to encourage the sale of appliances, as in the case of fuel-switching, the incentives in the present case are two-fold. One is the desire to help new subsidiaries gain a foothold in their market and then achieve high earnings. The second is the belief that subsidizing load management and conservation efforts is worth the cost to the ratepayers because it will avoid major expenditures for new generating capacity in the future. In either case, small businesses may face unfair or even anticompetitive situations.

2.3.3 Availability of Retained Earnings

La Follette [1984] and Sponseller [1985], among others, argue that, in contrast to the findings discussed above, many utilities actually have an
excess of retained earnings that they are attempting to invest in non-regulated activities. Recently, there has been a significant rise in utility earnings generally. These retained earnings, according to La Follette, originate from tax incentives and rate structures established in order to pay for future expansion needs in generating capacity. The logic behind these rates and tax incentives was that by charging higher rates and reducing taxes on certain utility investments now, ratepayers would not have to face sudden major rate increases in the future when new generating capacity is required. The actual result, however, is that utilities are flush with funds that they have decided to invest in acquiring new businesses. La Follette argues that the utilities should not be investing in new businesses, which are not liquid assets, but should be putting the retained earnings in preferred stocks and bonds. These investments can be more easily redeemed when funds are needed, whether it be for construction of new generating plants, or activities such as reducing acid rain or the decommissioning of nuclear plants.

The impact of utility diversification which has been motivated by the foregoing reasons on small energy-related businesses is only serious if the utilities are investing in the energy services market. Again, the possibility of cross-subsidization is the primary concern, since the utility management or the utility holding company may try to give the subsidiaries certain benefits that actually derive from access to the customer ratebase.

2.3.4 Economies of Scale and Economies of Scope

An economic argument, frequently used by government regulators, as well as utilities, to justify diversification is the availability of economies of scale and economies of scope. Both are efficiencies in production that are gained because a utility has certain underused resources or complementary relationships which may allow the utility to reduce its costs below that which competitors must charge. An example of an economy of scale is the availability of in-house staff at a gas utility that is underemployed during the summer months because gas use drops off significantly. This staff must be retained all year round, for reasons of job security, the cost of hiring, etc., so it is logical to use this personnel in work not directly related to the distribution of gas, such as providing home energy
audits or installing gas grills, during these slack periods. Although utility labor costs may be higher than average (due to the use of unionized workers, for example), these costs are covered in a utility's ratebase, making the cost of using this labor during slack periods for non-regulated activities very low. Economies of scope are gained by a utility investing in such things as its own fuel source, the means of transporting it to the distribution point or generating plant, and the means of eventual distribution. This type of integration can be more efficient than separate ownership.

Efficiencies gained through economies of scale or scope are regarded by most economists as a cornerstone of fair competition because they reduce costs through greater efficiency. Small businesses have no opportunity for achieving these same efficiencies, and, thus, the small businesses will lose in this type of competition.

The issue of economies of scale and scope raises two important points. First, utilities gain many economies of scale as a result of being regulated, not as a result of discovering better forms of production or having better management ideas. For example, the availability of underemployed resources, such as vehicles, at a utility is primarily the result of PUC requirements that the utility be able to provide secure, uninterrupted service to its customers. In order to do so, a utility must maintain a certain amount of excess equipment or staff to handle periods of high demand or unusual damage to the power system. In a competitive situation, this probably would not be the case. For example, a customer whose plumbing breaks down on a weekend may have to wait until Monday to have it repaired, or else pay a hefty premium to have a plumber perform a house call during off-hours. It could be argued, in turn, that utilities should seek more efficient ways to provide the level and reliability of service expected of them as a regulated entity, instead of being allowed to retain excess resources to meet unusual requirements, or to utilize these excess resources toward activities that benefit ratepayers more directly.

The second issue, which may have more immediate relevance, is the difficulty of determining if a utility is actually taking advantage of an economy of scale when it diversifies. This problem is similar to the cost allocation problem discussed in the preceding section on cross-subsidization in that a PUC must ensure that resources being shared with a subsidiary are
in fact underutilized by the regulated utility portion of the business. Therefore, a proper cost allocation system would have to start with a full examination of the types of resources to be shared in a proposed diversification plan. This system would supplement regular monitoring by the PUC to ensure that appropriate costs are being charged to the non-regulated subsidiary employing the resources.

2.3.5 Managerial Incentives

Malko points out that:

Utility executives see diversification as a means to attract better managerial talent. The diversified activities can provide managers with greater challenges and more opportunity for advancement than have traditionally been associated with the utility industry. [p.14]

Because of the traditionally slow growth of utilities and, to a lesser degree, the relatively narrow scope of activities involved in power generation and distribution, utilities may feel that they are unable to attract the highest quality managers. Thus, utilities may be diversifying, in part, to make the business more exciting, with higher rewards, in order to attract and hold better managers.

The question of managerial incentives is a significant one since they determine, to a large extent, how efficiently a utility will be operated. On the other hand, two points should be recognized. First, providing incentives through diversification does not guarantee that the regulated portion of the business will be better managed. In fact, managerial resources may actually be diverted away from the regulated utility in order to focus on the performance of non-regulated subsidiaries. Second, management incentives can be provided through means other than diversification. If utilities are not attracting the best management, this may be an indicator that better salaries and benefits need to be considered.

2.3.6 Government policies

Government programs, such as those established under the National Energy Conservation Policy Act (NECPA), will not receive substantial direct attention in this report, but it is important to recognize their impact. The Residential Conservation Service (RCS) and the Commercial and Apartment
Conservation Service (CACS), as well as many state and local programs, have
couraged, or even required, utilities to provide certain energy conservation
services, especially energy audits, and, thus, may have encouraged the
utilities to enter into other areas of the energy conservation services
market. Government-mandated programs, which are financed by the ratepayers,
and are thus a legal form of cross-subsidization, have generally been
justified on the grounds that the private sector is not providing sufficient
levels of service. However, since the private sector invariably responds
when the demand for services is high enough, the real problem may be the
lack of information and incentives available to consumers to encourage them
to undertake energy conservation measures. In fact, with the availability
of information and financial stimuli to consumers, business for many small
contractors and dealers has increased. Government policies may have,
therefore, designated utilities to implement these conservation programs
somewhat arbitrarily.

2.3.7. Summary

Several reasons are often given for utility diversification: to ensure
reliable energy demand and energy sources; lower utility earnings; availability
of retained earnings; economies of scale and scope; managerial incentives;
and government policies. Although none is the specific cause of illegal or
unfair cross-subsidization, each raises the potential that it could occur.
The primary motivation to cross-subsidize these diversified activities
arises out of a desire to increase sales, and thus the success of the
subsidiary activities.

2.4 Antitrust Legislation and FTC Jurisdiction

The nature of cross-subsidization and its impact on small businesses
has been thoroughly discussed in the preceding sections; however, the
restraints imposed on utilities involved in non-regulated activities by
specific antitrust legislation, i.e., the Sherman Act of 1890, the Clayton
Act of 1914, and the FTC Act of 1914, remain to be clarified.

Although most utility activities directly related to energy generation
and distribution come under PUC regulation, utilities have very few limitations
on their ability to diversify into non-regulated activities. One main
constraint is based on utilities' responsibilities to ratepayers, which, as
discussed in Section 2.5.3 on PUC Jurisdiction, are to ensure a secure
source of energy at reasonable prices. It is the purpose of PUCs to ensure
that these responsibilities are met, i.e., that non-regulated activities do
not disrupt service to utility customers. As mentioned above, this role may
include the imposition of accounting procedures to ensure that ratepayers
are not being required to support non-regulated activities which do not
contribute directly to the delivery of secure, inexpensive energy. As
noted in Section 2.5.2, utilities in certain states are also limited by
legislation which restricts their diversification activities.

At the national level, the major legal restrictions on utility diversi-
fication are embodied in the Public Utility Holding Company Act (PUHCA).
This act places utility holding companies under extensive review and disclosure
requirements of the Securities Exchange Commission. These requirements
provide a major disincentive to certain forms of utility diversification. In
fact, utilities have requested Congress to repeal or reduce these PUHCA
provisions.

Utilities, therefore, have the legal right, in most States, to diversify
into non-regulated activities. Once a utility diversifies, however, the
non-regulated activities are subject to the same antitrust legislation as
private business. Utilities' liability under the antitrust laws has only
recently been determined. Because of the state-action doctrine, "for some
time regulated businesses were generally thought to be exempt from antitrust
laws..." [Breed, 1982, p.3] However, Cantor v. Detroit Edison Co., 428
U.S. 579 (1976) narrowed the state-action exemption, making a utility
subject to antitrust laws "to the extent that it engages in business activity
in competitive areas of the economy" [FTC, 1982]. Furthermore, in California
Liquor Dealers v. Midcal Aluminum, (March 3, 1980, 63L Ed. 2d 233, 243)
the court made it clear that, if a State chooses to create a monopoly, that
decision must be "clearly articulated and affirmatively expressed as state
policy" and must be "actively supervised" by the State. [FTC, 1982] This
issue is not entirely settled, however, because in Grason Electric. et. al.
v. Sacramento Municipal Utility District (1985), the Ninth Circuit Court ruled
that a municipally owned utility is exempt from antitrust laws, on the
basis of government sovereignty.
Thus utilities' diversified activities are subject to prohibitions against such anti-competitive practices as price fixing, predatory pricing, tying arrangements, and other actions which may give the utility the ability to foreclose competition in the markets in which it operates. These prohibitions are primarily embodied in the Sherman and Clayton Acts, and the FTC Act, as mentioned above. The Sherman Act prohibits monopolization and attempts to monopolize, and "conspiracies in restraint of trade." The latter, found in Section 2, frequently involves price fixing, while the former, found in Section 1, involves companies with very large market shares, e.g., 70% to 90% or more of a particular market. The Clayton Act outlawed several specific practices, of which price discrimination and exclusive and tying contracts (Sections 2 and 3 respectively) are most relevant to this study.¹

Section 5 of the FTC Act states that "unfair methods of competition in or affecting commerce, and unfair or deceptive acts or practices in or affecting commerce, are hereby declared unlawful." [15 U.S.C. sec. 45(a)(1)(1976)] The general nature of this statement was intended to allow the FTC to "fill in the gaps" not covered by the Sherman or Clayton Acts, including incipient violations of those acts. In order to determine if a business activity has the potential for violating antitrust laws, the FTC "is empowered to make expert business judgments about the probable consequences of certain activities, and to prohibit those likely to result in future antitrust violations." [Averitt, p.229] In addition, the FTC can bring actions based on policies that it frames on its own initiative. This ability is significant to small businesses facing utility competition because it suggests that the FTC can order a halt to a utility action before an antitrust violation, under the other acts, actually occurs. Harm to the small businesses could thus be avoided.

In practice, antitrust cases have rarely been brought against utilities for attempting to monopolize in non-regulated markets, and even fewer by small businesses involved in the sale of energy-related services or products. One obstacle in bringing an antitrust case to court is the cost, which is prohibitively high for most small businesses. As demonstrated in the case

¹ The discussion of antitrust legislation is drawn largely from Public Policies Toward Business, by Clair Wilcox and William Shepherd (1975, pp. 112-113).
analysis sections, businesses have been more successful in bringing all types of suits when they have organized their resources in trade associations.

Furthermore, antitrust case is difficult to prove because of the nature of the energy services and products market, which is regarded by most experts as having very low barriers to entry. Because of these low barriers to entry, any business or entrepreneur with sufficient capital has very easy access to the market for energy-related services and products. Therefore, a utility which attempts to monopolize a market by reducing prices below cost, and thereby driving out competitors, will face renewed competition when it eventually raises prices back above its costs. In theory, utilities are dissuaded from attempts to monopolize the energy services market because they will be unable to gain monopoly profits.

From the point of view of small businesses, this theory does not help them in practice, however. A utility may lower its prices for energy services or products below cost for several reasons which are unrelated to the desire to increase the market share for its non-regulated activities. These reasons include efforts to promote fuel-switching to increase market share in the regulated side of the business, or to promote energy conservation in order to handle peak power demands and delay expenditures for costly new generating capacity. As mentioned earlier, utilities generally achieve these ends by encouraging the sale of high efficiency appliances or by installing energy conservation retrofits in homes and businesses. A utility may find that it must reduce prices substantially on these products or services to achieve a demand for these appliances or energy conservation retrofits that is high enough to influence the demand for electricity or gas. For example, a utility may determine that it must reduce demand for electricity in order to avoid building new generating capacity. For the utility, it may be worth subsidizing the price of conservation equipment and services up to the avoided costs for installing new generating capacity. In fact, many public policies, such as RCS, CACS, and state and local energy conservation programs, promote this type of subsidy. Small businesses, however, are likely to suffer as a result of these subsidized programs.

Where there is a stated public policy which requires or explicitly allows a utility to cross-subsidize energy conservation services and products, antitrust regulations do not apply, and small businesses must bring their
concerns to the public officials who established the policies. On the other hand, if a utility is cross-subsidizing a non-regulated activity without stated public approval, antitrust restrictions do apply. While small businesses rarely have the resources to bring a case against a utility, the above analysis of FTC jurisdiction does suggest that the latter can enjoin utility anti-competitive practices. Further, it has been suggested that an improper cross-subsidy harmful to small business competitors could alone be the basis for FTC action under Section 5 of the Federal Trade Commission Act as an "unfair method of competition" without regard to the existence of antitrust violations. [Herold, 1985]

2.5 Current Remedies

2.5.1 Anti-Trust and Fair Trade Practices

Since a fair amount of discussion has already been devoted to antitrust and FTC jurisdiction in the utility competition issue, it will suffice here to summarize the effectiveness of these as remedies for small businesses faced with unfair or illegal utility competition.

Overall, both remedies have distinct limitations. In the case of antitrust violations, although utilities are now generally regarded as subject to the Sherman and Clayton Antitrust Acts, small businesses must not only have evidence that a utility is illegally subsidizing products so as to sell them below cost, but the small businesses must demonstrate either an intent or the effect of driving them from the market. On one hand, the resources to gather this type of material are not frequently available to small businesses. On the other, it will be difficult to prove under most circumstances that the businesses have actually been shut out of the market. With very low barriers to entry, particularly in the energy services market, small businesses will be able to regain their market shares without much difficulty as soon as the utility raises its prices above cost, which it must do eventually.

In the case of the FTC, the problem seems to be primarily one of a lack of interest in prosecuting cases of this type. In conversations with FTC staff, it is apparent that, at this time, the FTC is not convinced of the harm caused by cross-subsidization or utility diversification. The
main argument given was that it benefits consumers and the economy if the utilities are able to provide products and services at lower cost, if these reductions are gained through greater efficiency, or the use of underutilized resources.

2.5.2 State Legislation

Through 1985, just four states have enacted legislation affecting utility entry into the market for energy producing or conserving appliances as seller, installer, or servicer: California, Wisconsin, Iowa and Minnesota. Legislation had been introduced in a number of other states, but not enacted, including Illinois, New Jersey, Michigan, Pennsylvania, Oregon, Mississippi, New York, South Carolina and Georgia. A brief summary of those bills compiled by the Alliance for Fair Competition is included as Appendix 2.

By and large, the legislation simply prohibits utilities from selling, installing or servicing energy appliances, except through an independent entity under certain restrictions. The bills pending in New Jersey, Mississippi, Michigan and Minnesota generally permit utility sales and services where the utility affiliate does not use the same premises, equipment, personnel or name and no cross-subsidy is maintained. Legislation in Pennsylvania bans all non-utility activity, and the South Carolina and Georgia bills prohibit the sale of satellite dishes by electric co-ops.

The law enacted in California (S.B. 1016, September 14, 1984) effectively precludes utility entry by prohibiting utilities and their subsidiaries from engaging in work which requires a contractor's license (work exceeding $200 in cost). Exceptions may be made where ordered or authorized by the commission in pursuance of other commission goals and the utility is permitted to contract the service with licensed contractors. By directing the Public Utility Commission to report to the Legislature "on policies, procedures and regulations adopted ... to ensure and promote competition in the energy conservation industry," the Legislature made its concern for the health of the energy conservation industry clear.

The California approach does not permit utility diversification even if it may be desirable from the point of view of the utility's economic health, non-prejudicial to utility ratepayers, with no chilling effect on competition. As might be expected, given the definitive work of Gregory Enholm and J.
Robert Malko of the Wisconsin Public Service Commission (PSC) in this area, the law enacted in Wisconsin (1985 Wisconsin Act 79, enacted November 19, 1985) allows for this possibility. Indeed, the law appears to address and resolve most of the thorny issues in the area with a sureness and simplicity bordering on elegance. The law requires utilities wishing to engage in activities outside of the generation and transmission of power to do so through non-utility affiliates held jointly with the utility in a holding company, with extensive PSC oversight.

The Public Service Commission will approve the establishment of such a holding company where:

1) transactions between the utility and non-utility affiliates are subject to PSC jurisdiction;
2) the non-PSC regulated activities do not substantially lessen competition;
3) the activities of the public utility affiliate remain under the jurisdiction of the PSC;
4) the new activities have no detrimental effect on utility rates or reliability;
5) the PSC has access to holding company records adequate for the regulation of the public utility affiliate; and
6) the provision of reliable and reasonably priced public utility service remains the predominant business of a public utility holding company system.

As part of the application for holding company certification, the legislation requires organizational documents explaining the relationships of the companies in the holding company, and specifically, the agreement between the public utility affiliate and any person with which it will be an affiliated interest in the holding company. Further, the application must include the identification of all public utility assets or information in existence, such as customer lists, which the applicant plans to transfer or lend to a non-utility affiliate. This submission must include the terms and conditions under which the transfer or use is proposed to take place. Perhaps most importantly, the law requires the applicant to disclose the method by which management, personnel, income, losses, costs and expenses
will be allocated within the holding company system between utility and non-utility affiliates.

By requiring access to holding company records and pre-approval of allocation formulae, the Wisconsin law allows the PSC to assure that utility cross-subsidization of non-utility affiliates has not taken place. In this regard, the law specifically prohibits the utility affiliate from lending to, or guaranteeing the obligations of, a non-utility affiliate. Further, the utility is prohibited from selling its services to its non-utility affiliates at a rate lower than that for the affiliate's class of customers. The non-utility affiliate may not use the utility name for competitive purposes. Sharing of employees between utility and non-utility affiliates shall have the prior written approval of the PSC, which will examine the burden of administering the arrangement in its approval decision. The utility is specifically instructed to provide its non-utility services in a manner that does not discriminate against competing providers. The legislation bars the utility from selling at retail, leasing, installing, maintaining, or servicing any appliance using the same energy source supplied by the utility except under three narrow circumstances or after PSC approval after notice and hearing. Finally, the PSC is also specifically instructed to aid small businesses in implementing these small business-related provisions.

In taking this approach, Wisconsin has recognized that diversification may be a legitimate business need of the utility. If the law is properly implemented by the PSC, diversification will not be at the expense of the utility's ratepayers or result in an unfair advantage to the new ventures over existing contractors. However, the Wisconsin Attorney General opposed the legislation, stating that he did not believe the PSC could exercise effective jurisdiction over a holding company under this bill. Others question the PSC's interest in implementing the new law.

The remaining enacted legislation in this area, in Minnesota and Iowa, seeks to protect small business with a more limited approach. In setting up a pilot program for utility provision of conservation services, the Iowa legislature (Senate file 450) specified that utilities provide competing bids of small businesses for the work that it proposes to do. The shortcoming of this approach is, of course, that without assurance that cross-subsidization
of the conservation services from regulated activities has not taken place, there is no way to know whether a low price set by the utility is fair to the competition.

The Minnesota approach (Minn. Stat. Ann. 216B.41 [West 1985]) also embodied in legislation establishing a pilot program to implement conservation improvements, is less specific. It stipulates that the Public Utilities Commission shall "provide ... for a free choice, by consumers participating in the program, of the device, method, or materials constituting the energy conservation improvement and for a free choice of the seller, installer, or contractor of the energy conservation improvement." Such strictures can be effective only with the implementation of an approach such as Wisconsin's that assures that the utility or utility affiliate is providing services at a price which adequately reflects its costs. To put it another way, "free choice" can be achieved only where the alternatives are fairly developed and presented to the consumer. Neither the Iowa nor the Minnesota legislation addresses this reality.

In conclusion, the Wisconsin legislation appears to address this issue with a comprehensiveness and workability that should make it a model for other states that have PSC's with adequate resources and interest to address this issue. States without extensive PSC staff need consider other approaches, such as restrictions on utility activity, or requiring public hearings at PSC's before initiation of utility diversification programs.

2.5.3 PUC Jurisdiction

Currently one means of redress that small businesses have available to them is to file complaints with state public utility regulators. However, as with judicial or legislative remedies, regulatory recourse is also limited in its effectiveness. This limited effectiveness largely stems from the fact that most PUC mandates assign responsibility primarily, if not solely, for overseeing the interests of ratepayers, as opposed to outside interests such as small businesses. As Charles Gray of NARUC points out in his testimony to the House Subcommittee on Antitrust and Restraint of Trade Activities Affecting Small Business [Oct., 1983], PUCs have two main responsibilities regarding utility diversification:
1) to ensure that the ratepayers of monopoly services are not called upon to subsidize nonregulated utility businesses, and 2) to ensure that the diversified business activities of a utility do not threaten the financial integrity of the company's utility business. [p.179]

However, the extent to which a PUC sees its responsibilities can be a relative matter. According to Gray,

many States have so-called ‘affiliated interests’ authority, which enables the respective State commissions to prescribe special accounting and reporting requirements for transactions between utility affiliates. [p.181]

For example, PUCs in Maine, Montana, and New Mexico have the legislative authority to review all affiliate transactions; the Wisconsin PUC has the authority to review any proposed reorganization, for example, into a holding company; and PUCs in Massachusetts and Washington have jurisdiction over the formation of holding companies if done through mergers [Sponseller, 1985]. In Rhode Island and Nevada, the authority to review affiliate transactions is limited to initial mergers involving nonutility business; however, in this case, the authority does not continue once the merger is effected. On the other hand, many states do not endow PUCs with this degree of authority.

Problems also arise because certain PUCs may not be fully aware of their authority or may not wish to test its limits. For example, some PUCs may not be fully cognizant of the fact that utilities can be subject to Federal antitrust scrutiny, as explained in section 2.4. This lack of familiarity on the part of some PUCs with current laws or precedents is a matter of concern to small businesses who may be the victims of serious antitrust violations. This was the case under the long-standing state-action doctrine, which has recently been revised. Although the Cantor case made it clear that public utilities are subject to the same antitrust legislation as private businesses, some PUCs continue to operate under the impression that utilities are still exempt from antitrust legislation. In addition to the limits on the state-action doctrine, other precedents that PUCs may be unaware of exist which could also serve as grounds for restricting utility competition in the private market. For example, in Northern California Power Agency v. Public Utility Commission, (1971) and Oil Heat Institute v. Anchorage National Gas Corp. (1967), the question of "public interest" was a deciding factor. In the first case, the court found that "the public interest in preventing monopolies is one facet of the larger public convenience
and necessity which the Commission was established to protect." In the second case, the PUC found that acts which "violate all ordinary precepts of conscionable activity and fair play" are against the public interest and therefore should be restricted or denied. It might also be noted, that some PUCs have been given the authority under state laws to make determinations regarding utility diversification through "public interest" provisions. [FTC, 1982]

Thus, small businesses seeking a remedy through PUCs for unfair or anticompetitive actions on the part of utilities must ask two questions before bringing their complaints before a PUC: 1) to what extent will the PUC use its authority to oversee utility diversification efforts, and 2) to what extent is the small business's complaint relevant to all ratepayers?

Regarding the first question, a small business wishing to bring an action against a utility would benefit initially by determining the PUC's actions in other complaints of a similar nature. Not only could the small business obtain an idea of how to present a complaint in order to gain the PUC's attention, but it could also obtain information on cases which set useful precedents that would strengthen the small business's own arguments.

If this process identifies an approach that succeeds in raising the interest of the PUC, and possibly even motivates the PUC staff to initiate a review without a formal complaint or rate intervention request, that would be fortunate. However, it is also possible that the PUC would be reluctant to handle problems of cross-subsidization or other unfair practices, or it may turn out that such a complaint has never been raised before, and therefore no positive precedents would be available on which to base arguments.

In these cases, the business has at least a couple of alternatives. First, it can raise the idea with the commissioners and their staffs in order to obtain a preliminary indication of support. If a positive indication is given, the business may wish to proceed with the complaint. If the indication is not positive, the business may opt to bring political pressures to bear on the PUC either through lobbying efforts with other State officials, such as the State legislature, or through direct appeal to the public, especially utility customers.

Regarding the second question, namely the relevance of a complaint to ratepayers, all studies indicate that small businesses or small business
associations are most successful at bringing complaints that also have a direct bearing on ratepayer interests. Illegal cross-subsidization, in particular, would thus be grounds for PUC action, due to the fact that improper cross-subsidization of a non-regulated subsidiary by a regulated utility may result in ratepayers bearing costs for which they are not responsible. This type of complaint can be brought as a rate intervention during PUC rate hearings. A small business can point out to the PUC that certain costs requested by the utility should not be allowed because they are incurred by non-regulated subsidiary activities for which ratepayers either run an unnecessary risk or do not receive any direct benefits. The PUC is not, then, dealing directly with the question of fair or unfair competition, but the PUC action may nevertheless halt a utility practice that is harmful to the small business.

In summary, PUC jurisdiction and interest in small business complaints will vary depending on a number of factors. The most important point to recognize is that PUCs are primarily responsible to ratepayers, and they may not have the authority or the resources to respond to complaints about utility activities that do not harm ratepayers. This does not mean, however, that small businesses have no recourse to PUCs. Many of their complaints are also of interest to ratepayers, and, if properly presented, PUCs are likely to respond favorably. As the cases covered in the General Case Analysis and Key Case Analysis sections illustrate, the sharing of costs between regulated and non-regulated activities is of particular concern to PUCs. Based on the cases studied, commissions appear to react positively to complaints which clearly demonstrate that utility activities which can be shown not to be an obligation necessary for providing safe and inexpensive energy are nevertheless being charged to the ratebase. Although the decisions do not generally award damages for past actions, they do commonly require utilities to allocate costs properly for each type of non-distribution activity in which they are engaged and to charge customers directly for those which are not a utility obligation.
3.0 GENERAL CASE ANALYSIS

This section analyzes 12 legal proceedings brought by small business contractors against electric or gas utilities. These proceedings illustrate a variety of conflicts between small businesses and utilities over the unregulated business activities conducted by many utilities. The purpose of this section is to summarize the proceedings, determine their similarities and differences, and to analyze the decisions brought by the courts or the Public Utility Commissions. A chart of the 12 cases is presented on the following page.

3.1 Description of Proceedings and Issues Raised

The proceedings encompass three broad issues of concern to small businesses: utility cross-subsidization, monopolization and miscellaneous diversification issues. Contests containing allegations of utility cross-subsidization were most prevalent, involving 6 of the 12 proceedings. In the cross-subsidization proceedings, the contractors claimed that utility resources and revenues from regulated portions of their business helped to support or subsidize unregulated utility operations (e.g., sales, installation and service of appliances). See Sections 2.1 and 2.2 for further discussion of cross-subsidization.

The issue of attempted utility monopolization of markets outside their regulated operations was raised in 3 of the 12 proceedings. These three cases allege that both the Sherman and Clayton Antitrust Acts, which govern "unreasonable" restraint of trade and use of monopoly power in one market (i.e., the utility's regulated market) to gain unwarranted competitive advantage in another, were violated. See Section 2.4 for further discussion of the Federal antitrust laws.

Public Utility Commissions had jurisdiction for all but three of the proceedings analyzed. With the exception of one rate case intervention, all proceedings heard by PUCs involved formal complaints lodged by contractors. In these proceedings, the complainants all sought the scheduling of hearings on the issues and a PUC order that would modify the utility's behavior.
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<td>2. Sheet Metal and Air Conditioning Contractors National Association v. Laclede Gas Company</td>
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<td>12. William F. Ward v. Toledo Edison Company</td>
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Jurisdiction for the three proceedings which alleged violation of Federal antitrust laws, lay in the Federal Courts. In these cases, the plaintiffs sought treble damages for the alleged violations.

3.1.1 Utility Cross-subsidization

Five of the six cross-subsidization proceedings involved gas utilities. These proceedings all involve allegations of cross-subsidization of gas appliance sales, installation and service.

In three cross-subsidization proceedings (Sheet Metal Contractors of Idaho v. Intermountain Gas Co. (Intermountain Gas), Sheet Metal and Air Conditioning Contractor National Association v. Laclede Gas Co. (Laclede 1) and Johns Plumbing Repair Co. v. Piedmont Natural Gas Co. (Piedmont)) the complainant’s principal allegation was that the pricing of gas appliance sales, installation and service is artificially low due to cross-subsidization from the utility’s regulated operations.

In Intermountain Gas, a trade association filed a complaint with the Idaho Public Utilities Commission in March 1976 that requested a hearing to review the utility’s practices, which were alleged to be "discriminatory and prejudicial"; furthermore, the PUC was requested to order the utility to "cease and desist from engaging in the business of installation, repair, maintenance, and servicing of gas appliances." No specific statutes were invoked by the complainants in this broadly worded complaint.

In Laclede 1, a trade association intervened in May 1983 in a utility rate case. In this rate case, the intervenors sought to have expenses related to the utility’s gas appliance business disallowed from their requested rate increase.

In Piedmont, the complainant, Johns Plumbing, (a private plumbing contractor), asked the North Carolina Utilities Commission in July 1980 to order the respondent to "discontinue renting, selling, installing, and servicing water heaters at less than fair market value." The complainant also requested that a public hearing be held on this complaint to determine damages suffered "as a result of the practices and policies of [the respondent]."

In the case of Mid-Atlantic Petroleum Distributor’s Association v. Baltimore Gas and Electric Co. (Baltimore Gas), the complainant charged
in September 1983 that the utility was violating specific Maryland statutes governing promotional practices by utilities. The complaint did not allege directly that cross-subsidization had occurred; however, it did indicate that rebates, market financing, and "free" three year service policies were offered to customers who agreed to convert from oil space heating to gas space heating. These practices suggest that Baltimore Gas was engaging in cross-subsidization. The relief requested by the complainant included the issuance of an order to stop the utility's Gas Heat Conversion Program, an investigation by the PSC staff and an informal hearing on the issues.

In the case of the Alliance for Fair Utility Competition v. Washington Gas Light Co. (Washington Gas) the Alliance alleged in May 1984 that the utility engages in cross-subsidization of all nine of its wholly-owned subsidiaries. Washington Gas subsidiaries engage in a wide range of activities, from energy exploration to energy conservation services. The complainants specifically charge the utility with violating Maryland Public Service Commission Law and the Uniform System of Accounts. The complainants requested the issuance of a Show Cause Order requiring the utility to respond to the allegations and conduct of both a hearing on, and an investigation of, the issues.

One proceeding which raised the issue of cross-subsidization involved an electric utility, Mike Perry v. Florida Power and Light Co. (FPL). In this proceeding, Mike Perry, an air conditioning and refrigeration contractor, alleged in November 1983 that the utility's "Energy Store" was cross-subsidizing its sales, a charge which was not refuted by the utility. The Energy Store was established by Florida Power and Light to sell and promote energy conservation devices. Mr. Perry specifically charged that the utility's "Energy Store" was not cost-effective under the Florida Public Service Commission Rule 25-17-.08. The complainant requested that the Florida PSC order a hearing to consider closing the Energy Store.

The proceedings which raised cross-subsidization issues were similar. All of the analyzed proceedings were under the jurisdiction of Public Utility Commissions, and all requested, as part of their relief, a hearing and an order modifying utility practices.
3.1.2 Antitrust and Monopolization

In John Hicks, et al. v. Public Service Company of Oklahoma (PSC of Oklahoma), a group of small businessmen engaged in the leasing of commercial and industrial outdoor lighting brought an action in 1983 alleging utility violations of the Sherman and Clayton Antitrust Acts. Specifically, the utility was alleged to have attempted to drive its competitors from the outdoor lighting market, by pricing its own outdoor lighting below its own cost, by denying the plaintiffs' access to dawn electricity and by unfairly raising the price of electricity to the plaintiffs.

In Control Temp Consultants, et al. v. Detroit Edison Co., et al. (Detroit Edison), a group of small businessmen, engaged in the provision of energy conservation services to residential and commercial customers, brought an action in October 1983 alleging that a group of large Michigan utilities violated the Sherman and Clayton Antitrust Acts. The plaintiffs charged that the subsidized residential energy conservation audits offered by the defendants under the Federally-mandated Residential Conservation Service Program were unfairly priced. Residential audit prices were set at $15. The defendants also charged that the defendants took advantage of their "exclusive franchise" as utilities and their obligations under the RCS Program to also offer commercial energy audits at unreasonably low prices, thus "unfairly" competing with the plaintiff's businesses.

In Grason Electric Co., et al. v. Sacramento Municipal Utility District (SMUD), a group of electrical contractors brought suit against a publicly owned utility in 1981, claiming that it violated the Sherman and Clayton Antitrust Acts. Specifically, the plaintiffs alleged that the utility had unlawfully used its State-granted monopoly power in the retail electric energy market as to preclude plaintiffs from obtaining work constructing electrical distribution systems. These systems include all electrical distribution wiring for a property which requires new electrical service. The plaintiffs contended that they could not penetrate this market (electrical hookup of new homes) because of the defendant's market presence. The plaintiffs additionally alleged that the utility engaged in monopoly leveraging of electrical distribution systems using its sanctioned monopoly power in electric power generation and distribution.
The three antitrust cases, PSC of Oklahoma, Detroit Edison, and SMUD, while possessing different facts and issues, bore a common thread as actions brought under the Federal antitrust laws. All three cases charged monopolization and restraint of trade by the utilities and requested treble damages for each alleged violation.

3.1.3 Miscellaneous

Three proceedings analyzed in this section are not easily categorized. One such proceeding is Master Plumbers Council of New York City v. Brooklyn Union Gas Co. (Brooklyn Union). In September 1982 the complainants sought to force the utility to obtain a "test card" from the New York City Department of Buildings before the utility can turn on the gas supply or restore the gas supply as a result of gas piping work. A test card is a detailed check-out sheet that provides guidance to plumbers when they are in the final stages of gas service provision or restoration. The issuance of a test card requires the presence of a licensed plumber and an inspector from the New York City Department of Buildings. The Master Plumbers Council petitioned that a declaratory order be issued under the State's Administrative Procedure Act and the Rules of Procedure of the Public Service Commission.

In Marco Sales v. Laclede Gas Co. (Laclede 2), a heating/air conditioning contractor alleged in September 1981 that the gas utility unlawfully imposed a new surcharge rate against customers which installed "add-on" electric heat pumps in an attempt to discourage the use of these devices. This additional charge amounted to approximately $15.00 per month. The complainant requested that an order be issued that would curb the alleged illegal practices.

In William F. Ward v. Toledo Edison Co. (Toledo Edison), a heating/air conditioning contractor alleged in April 1983 that the utility was engaging in unfair competition by excluding some contractors from its subsidized electric heat pump inspection program. Mr. Ward specifically charged the utility with violating several Ohio Statutes which were under the jurisdiction of the Ohio Public Utilities Commission. The relief requested by the complaint included the convening of a hearing, investigation, of the allegations and the issuance of a "cease and desist" order by the PUC.
3.2 Decisions

3.2.1 Nature of Decisions

The decisions rendered in the actions described above span a wide range. In the seven proceedings where final decisions were reached, four were rendered against the contractors.

In PSC of Oklahoma, where outdoor lighting contractors charged monopolization of the outdoor lighting business by the utility, the U.S. District Court for PSC of Oklahoma ruled against the contractor plaintiffs for two reasons. One, the plaintiffs failed to prove that defendant's wrongdoing caused harm to the plaintiffs, and two, the plaintiffs failed to prove that the defendant's wrongful acts occurred in interstate commerce or had any effect upon interstate commerce. However, the case was overturned by the U.S. Court of Appeals. The U.S. Court of Appeals decision found that the defendant was guilty of refusing to sell the plaintiffs dawn-to-dusk electricity, refusing to let the plaintiffs use the defendant's poles to mount lights, delaying the plaintiffs electrical hook-ups and implementing a price structure that was "very discriminatory against the plaintiffs" and remanded the case to the District Court for final action. The final decision in PSC of Oklahoma has not been rendered as of this writing.

Of the proceedings where the contractors did not prevail, two decisions (Laclede 1 and Intermountain Gas) were decided for the utilities because the PUCs viewed the records generated in the proceedings as inadequate to resolve the disputes. Intermountain Gas stemmed from a PUC complaint and Laclede 1 stemmed from a PUC rate intervention.

Laclede 2 was ultimately decided in favor of the complainant. The initial decision issued by the Missouri Public Service Commission in December, 1981 was that the utility had not filed the necessary tariffs to enable it to impose a surcharge on add-on heat pump customers. This decision was overturned by the Missouri Circuit Court on technical grounds, however, it was appealed to the Missouri Court of Appeals. On December 4, 1984, the appeals court upheld the finding of the PSC that the utility had not presented sufficient evidence of a need for the surcharge. Although this decision was appealed to the State Supreme Court, the latter refused to hear the case, letting the decision of the PSC stand.
In Detroit Edison, the U.S. District Court for the Eastern District of Michigan dismissed the suit on Sept. 2, 1983, brought by the energy conservation service contractors against the major electric and gas utilities in Michigan. In reaching its decision, the court concluded that "conduct alleged [by the plaintiffs] is compelled by and taken pursuant to a federal statute." The statute referred to is the National Energy Conservation Policy Act, 42 U.S.C. Sec. 8201 et seq., which requires major electric and gas utilities to offer residential energy conservation audits at subsidized prices.

In Washington Gas Light, the hearing examiner dismissed the case, in May, 1986, on the recommendation of the complainants. The latter based this recommendation on further information provided by WGL which explained the utility's procedures in dealing with its subsidiaries and on changes in the utility's policies which would ensure the total separation of utility activities from non-utility activities.

In Baltimore Gas, the Maryland Public Service Commission rejected, in June, 1983, the claims of the fuel oil distributors which charged the utility with violation of the PSC rules governing utility promotional practices. The PSC determined that the proceeding was moot, as these PSC rules on utility promotional practices were changed shortly after the filing of the complaint. The utility was not in violation of the revised rules and the complainants chose not to pursue their complaint further.

In Brooklyn Union, the New York Public Service Commission ruled in May, 1983 against the Master Plumbers Council and refused to issue the requested declaratory order requiring the utility to obtain "test cards" for certain types of gas line work. The PSC, in issuing this decision, made note of ongoing negotiations between the utility, Master Plumbers Council and the New York City Department of Buildings to resolve the dispute. It appears that the PSC chose to wait and see if the dispute could be settled in another forum, rather than involving itself in the matter.

In FPL, the Florida Public Service Commission terminated the proceeding in April, 1984 upon the consent of all parties. After the complaint was filed by Mike Perry alleging that the utility's "Energy Store" was not cost-effective (and before any hearing was held), the utility voluntarily decided to close the store. In this proceeding the complainant relied on testimony by the
utility during its previous rate increase request, which stated that the utility's average cost for each order placed at its Energy Store was nearly $28, while the average charge for each order was only $15.

The Toledo Edison proceeding (1985) was settled by the parties. The settlement added the names of the complainant contractors to the list of "approved" contractors eligible to participate in the utility's subsidized electric heat pump inspection program.

3.2.2 Proceedings Without Decisions

Several of the proceedings analyzed in this chapter have not yet yielded a decision. These unresolved proceedings are still ongoing or on appeal at the time this study was prepared.

In one proceeding, Piedmont, the complainant apparently stopped work on the proceeding due to lack of funds. The complainant, Johns Plumbing, spent approximately $10,000 in legal fees before the North Carolina Association of Plumbing- Heating- Cooling Contractors agreed to pursue the complaint. Shortly after the legal responsibility for litigating the complaint was transferred, the Association's attorneys simply stopped pursuing the proceeding. The PUC docket in Piedmont has remained open since early 1982; there is no indication that the Association intends to begin litigating this complaint again.

In SMUD, after the utility prevailed in U.S. District Court, which ruled that SMUD was not immune from the antitrust laws, the defendant prevailed on appeal to the Court of Appeals. The Appeals Court held on September 4, 1985 that because the utility is a government agency it is exempted from Federal antitrust laws. The plaintiffs appealed to the U.S. Supreme Court to overturn the Appeals Court decision. The Supreme Court recently declined to review the case, leaving intact the lower court's decision.

3.2.3 Resolutions

As noted previously, a court or PUC has ruled against a utility in only one proceeding (PSC of Oklahoma) analyzed in this chapter. Damages were awarded in the this outdoor lighting monopolization case by the
U.S. District Court in favor of the plaintiff contractors. However, the trial court has not yet ruled on post-judgement motions.

Only in one analyzed proceeding, Toledo Edison, did a contractor and a utility settle out of court. In this proceeding, where the complainant charged the utility with unfairly barring them from the list of contractors approved for the utility's heat pump inspection program, the utility agreed to place the complainants onto the list of approved contractors.

In two proceedings, the utilities withdrew voluntarily from the activities which were under complaint. In FPL, the utility decided to voluntarily close its Energy Store before the hearing to probe its cost-effectiveness could be held. In Intermountain Gas, the Idaho Public Utilities Commission ruled against the complainant contractors. The PUC found the record inadequate to rule for the complainants. Nonetheless, the utility subsequently chose to withdraw from the gas appliance business.

From the survey of former contractor complainants in the proceedings where the contractors did not prevail, it is clear that the utilities have not modified their practices for which the contractors originally brought action. Only in Toledo Edison, FPL and Intermountain Gas (outlined in the previous paragraphs) have the utility's business practices been modified to alleviate contractor concerns. When a final decision is issued in PSC of Oklahoma, the utility may be under court order to modify its practices.

It is clear from the analysis of these 12 proceedings that neither Public Utility Commissions nor the courts have generally acted to alleviate the concerns of small business contractors regarding "fair" competition with utilities. The filing of legal complaints, interventions or lawsuits by contractors has proven ineffectual in restraining utility ventures into unregulated enterprises, with a few exceptions. However, the following five case studies suggest that a reasonably well defined rate intervention, particularly with the aid of a sympathetic PUC staff, can obtain relief against improper cross-subsidization.

3.2.4 Addendum

As this report was in its final stages, information on two important cases of cross-subsidization became available which are briefly described below.
Michigan Consolidated Gas Company - In 1984, Michigan Consolidated Gas Company initiated an appliance maintenance program. For a yearly fee, the company inspects or repair furnaces and water heaters without any additional charge depending upon the type of program the customer has selected. The heating contractors submitted testimony in an October, 1984 rate hearing, complaining that the program was subsidized. Their contention was not addressed by the Administrative Law Judge since they appeared at the proceeding too late to intervene formally as a party. The PUC, in its June 1985 opinion, specifically advised MichCon to assure against ratepayer cross-subsidies.

A Public Service Commission staff audit in Fall 1985 subsequently determined that the accounting was "loosely maintained and needs improvements." It found deficiencies in three areas:

1. Failure to reconcile the internal accounting records;
2. Inadequate attention paid to overhead rates; and
3. Inappropriate timekeeping practices.

For the first year of 1984-85, the company claimed a net income after capital costs and taxes of $239,107 on an income of $1,783,011. Commission staff reduced the net income to $131,643 (resulting in a return of about 7 percent instead of 13 percent).1

Montana-Dakota Utilities - Montana-Dakota is an electric and gas utility engaged in the sale of appliances, the installation and repair of appliances, and the installation of customer-owned piping. The Public Service Commission of North Dakota initiated a staff audit of the merchandising operations after receiving complaints from several appliance dealers. In a February 1986 rate case decision, the Commission agreed with staff that the merchandising accounting was "less than meticulous in ensuring that all expenses related to merchandising are treated below the line." [p. 9] It directed the utility to revise its allocation of building space-related

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1 PSC Staff Report, "Appliance Maintenance Contract Program Investigation," undated. It is interesting to note that the staff reports that "The program is not being subsidized by the ratepayer. On the contrary, the ratepayer is being helped." This conclusion was based on the observation that sharing of joint costs provides ratepayer savings that otherwise would not occur (i.e., through economies of scale). However, improper allocation of joint costs is still cross-subsidization and unfair to the ratepayer.
expenditures (joint costs) and depreciation expenses and to charge the merchandising operation with a share of the cost of company-provided utility services, namely gas which it was receiving for free. [p. 9]
4.0 KEY CASE ANALYSIS

4.1 MINNESOTA GAS COMPANY

Twin Cities Piping Industry Association (Twin Cities) and SMARCA of Minnesota, Inc. (SMARCA) petitioned to intervene in a rate request filed by Minnesota Gas Company (Minnegasco) on August 29, 1980 for a 9.2% ($28.3 million) increase in gross annual revenues. The intervenors claimed that Minnegasco charged some of the costs of its customer appliance service program to the utility's natural gas rates rather than charging customers for the cost of service calls. Twin Cities and SMARCA were supported in their claim by the Minnesota Department of Public Service.

4.1.1 Legal Jurisdiction

Because the complaint was raised as a rate intervention, the Public Utility Commission clearly had the jurisdiction to decide the validity of the intervenors' arguments. Although there was no issue concerning the PUC's overall jurisdiction, Minnegasco argued on rehearing that the PUC could be guilty of unconstitutional and unlawful ratemaking in two specific instances. Minnegasco argued, first of all, that the PUC's right to examine rates is limited to the proposed rate schedules that are the subject of the specific rate request. Since the utility was not asking for changes to the rates that cover its customer appliance service program, it argued that the PUC did not have the authority to examine that specific account. Furthermore, the utility argued that the Commission had already approved the service program expenses in previous rate hearings and that circumstances had not changed which would invalidate those expenses.

Second, the utility argued that by invalidating the expenses for the service program back to the start of the test year rather than on a prospective basis, it was guilty of retroactive ratemaking, which the utility claims is confiscatory, inequitable, and "universally" regarded as unconstitutional and unlawful.

4.1.2 Description of Case

Several specific issues were raised by Twin Cities, SMARCA, and the Department of Public Service (DPS), on the one hand, and by Minnegasco, on
the other. They generally centered on the difference between emergency services, such as leak investigation, and customer appliance services. The latter included appliance hook-up, maintenance, and inspection. Although some service calls were billed directly to customers, many were simply charged to the natural gas rates.

**Intervenors**

In order to establish the need for a closer examination of Minnegasco's customer appliance service program by the Commission, the DPS began by pointing out that Minnegasco's customer installation expense as a percentage of its total distribution operation expense was 53%. Comparable figures for other utilities ranged from 6% to 39%, with an average of 23%. This unusually high percentage in Minnegasco's case clearly indicated the need to examine Minnegasco's service charges. It was found, in fact, that 64% of customer service calls were not charged to the customers, again a high percentage according to the DPS.

In its investigation of Minnegasco's books, the DPS identified several overhead charges for the service program that were billed to the utility's natural gas rates. These charges included a computer dispatching network, a recordkeeping system, training facilities, engineering support, repair part inventory, billing and accounting, and supervision and management support. The DPS, along with Twin Cities and SMARCA, argued that these charges were an unfair burden to ratepayers because they subsidized customers who used the program. Such a subsidy creates an unfair preference, meaning customers are given special treatment or are forced to pay higher rates than other customers.

Twin Cities and SMARCA contended, furthermore, that contractors are harmed by the utility's use of its monopoly power. [Petition to Intervene, para.6] By using its ratebase to subsidize a non-regulated utility function, the utility is cross-subsidizing its service program.

**Utility**

Minnegasco made three main arguments to support its contention that the appliance service revenues and expenses should be included in the natural gas rates.

First, the utility claimed that it had an obligation under Minnesota law to provide the service program. This argument centered primarily on the issue of customer safety, which could be threatened if service calls
are charged to customers. Minnegasco claimed that "dangerous and unsafe conditions may result from customers trying to avoid a service charge," and, therefore, it was Minnegasco's obligation to provide the service. The intervenors offered the rebuttal that the safety record of NSP in St. Paul, where service calls are charged directly to customers, is comparable to Minneapolis. The DPS in particular stated that Minnegasco did not offer sufficient evidence to show that safety would be threatened. In addition, the intervenors noted that an appliance service program is not a necessary part of gas distribution responsibilities. A utility's obligations are "...the installation, removal, or repair of equipment or facilities for delivering or measuring such gas and electricity." [M.S. sec.2168.02, subd.6.] In other words, a utility's responsibilities end at the meter.

The second main argument offered by Minnegasco was that the service program is a "historic business practice" because it has been offered for many years. Out of "contract and custom with the communities served" the utility has the responsibility to continue the service, according to Minnegasco.

Finally, Minnegasco argued that there was overriding public support for the service program. The Suburban Rate Authority supported Minnegasco in this claim.

4.1.3 Decision

The Commission issued its first order in August 1981 and, after reconsideration, a second order in November 1981. The following discussion covers both decisions, since only one change was made in the second order.

Specifically, the Commission ordered Minnegasco to charge all non-emergency service calls to the customers requesting the service. It also reduced the operating expenses by $4,097,000 to account for service program expenses and depreciation expense on a portion of the Linden Office Building, which housed the service center. In addition, the Commission removed from plant in service the portion of the Linden Office Building used for the service.

In its reconsideration, the Commission did reverse itself on the disallowance of appliance service program expenses back to the start of the
test year. It found that it was not practical to charge retroactively customers who used the program during the test year.

In reaching its decision, the Commission drew several conclusions:

- A utility is not obligated to provide customer appliance service. The Commission stated in its findings that "the servicing of customer appliances which consume gas is clearly outside the scope of delivery or measurement at the customer's meter."

- The safety issue is important; however, the utility is not being required to halt any services that would threaten safety. Leaks and emergency repairs continue to be billable; only the costs of other services must be recovered directly from customers using the service.

- The service program creates an unreasonable rate preference. The Commission pointed out that it has always moved to eliminate unreasonable cross-subsidies where non-cost factors are involved. In dismissing Minnegasco's claim that charging for the service would place a burden on the elderly and poor, the Commission stated that no difference, in their ability to pay, exists between customers who use the service and those who do not.

- A utility that requests a rate review subjects all its rates to potential scrutiny. Therefore Minnegasco's claim that the PUC had no authority to review utility accounts that were not specifically a part of the utility's rate request was also dismissed.

- Based on evidence presented at the hearings, the hearing examiner concluded that there was a split between customers expressing support for the program and those concerned with unfair preferences and cross-subsidization. Thus, the Commission determined that there was no clear consensus regarding customer support for the service program.

4.1.4 Conclusions

The Minnegasco case represented a major success for small contractors by forcing the utility to charge a fair and reasonable price for non-emergency services, and by reducing its operating expenses for those services. The order also left no doubt that the utility could not bill overhead charges.
for the service to its ratebase, or include in its plant in service those facilities used for the service. While the PUC's order did not preclude the utility from the appliance service market, or specifically restructure it accounting system, as long as the utility's accounts are reviewed regularly, it will be difficult to cross-subsidize appliance services, which will allow contractors to compete on more equal grounds with the utility:

Overall, the contractors' success in this case is due in part to the fact that the complaint was brought as a rate intervention. In a rate intervention, the PUC staff has to provide much of the relevant background research. This research can be extremely important to contractors with limited resources. Equally as important, the burden of proof rests with the utility, which must justify its charges in a rate intervention. Although complainants must justify their claims, it is up to the utility to disprove them. As a result, burden on contractors is eased. The only drawback to bringing a complaint through a rate intervention is that contractors must wait until a rate review is requested by the utility. It is quite conceivable that a utility will not ask for a rate review for some time, leaving contractors little opportunity to end the anti-competitive activity.

Emphasizing the issue of unfair preference may also have been a wise decision as it is an important ratepayer concern that is within the Commission's authority to proscribe. The issue of unfair competition, which the two contractor associations raised, was not considered a matter that the PUC may decide. In fact, their argument was never discussed in the Commission's findings.

In sum, the contractors were very fortunate to have the DPS on their side throughout the case. Its research of the issues and the utility's accounts clearly helped persuade the Commission.

In a follow-up call to Twin Cities, it was learned that Minnegasco had decided to provide the non-regulated customer services through a separate subsidiary. In doing so, the subsidiary found that it could not compete with the members of Twin Cities, who are primarily involved in the commercial area, and thus withdrew from that market. The utility charged $21.50 to residential customers for the initial hour of service in 1979. After the decision in this case, Minnegasco changed its rates on December 1, 1981 to $30 for the initial half hour and $42 per hour additional. On the other
hand, SMARCA is not satisfied with the results of the case, arguing that Minnegasco continues to cross-subsidize its customer services. This is very difficult for the association or its members to prove, however. SMARCA is therefore pressing for legislation that would specifically prohibit all utility cross-subsidization of non-regulated activities. The bill would prohibit sharing the use of premises, equipment, inventory personnel, or other utility resources. Utility affiliates are also precluded from using the utility's name. The association believes that legislation would make oversight and review of the utility's activities easier and more effective.

4.2 ALABAMA GAS CORPORATION

In 1983, Alabama Gas Corporation (Alagasco) renewed a program, which it conducted prior to 1971, to sell, service, and install gas grills. In May of 1983, Alabama Gaslight and Grill, Inc. (AGL&G), a supplier and installer of gas grills, filed a complaint with the Alabama Public Service Commission (PSC) alleging that Alagasco was not charging customers for the full cost of grills or their service and installation. A hearing was requested before the PSC in June, but the case was dismissed with no hearing granted.

4.2.1 Legal Jurisdiction

The PSC's stated policy is not to involve itself in any utility merchandising activities. It does, however, reserve the right to examine all utility accounts during a rate request in order to ensure that there is no cross-subsidization of non-regulated activities.

4.2.2 Description of Case

The central issue in the case was whether Alagasco was charging the full cost to its gas grill customers or whether it was subsidizing certain costs by charging them to its ratebase.

Intervenors

AGL&G based its charges against Alagasco on the argument that the price being charged by the utility was significantly lower than that charged by other utilities in the region for comparable grills. AGL&G complained that the only way the utility could do this was by charging part of its

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operational costs to its ratebase. The costs which were not recouped through its prices, according to AGL&G, included inventory, service warranties, accounting costs, advertising costs, insurance, supervisory expenses, employee time involved in sales and promotion, and utility financing services. With regard to the latter, the utility offered financing at 14% for 36 months; according to AGL&G, this financing was not available elsewhere.

AGL&G argued its case primarily on the basis of Title 37-1-36, which holds that non-utility business must "assume or bear full costs." In other words, utilities may not cross-subsidize non-utility activities. Such cross-subsidization constitutes "rank discrimination."

Utility

Alagasco would not disclose its schedule of costs for the grills, accessories, or installation costs, but it asserted that its prices did include the costs for warehousing, inventory, and warranty coverage. In addition, Alagasco claimed that its price for one particular grill was approximately $70 more than that charged by AGL&G for a comparable grill; and therefore, it could not possibly be harming the sales of AGL&G.

The utility also argued that the sale of grills was necessary to compensate for declining gas sales and to compete with other energy sources. The utility made the point that these sales benefited ratepayers because increased utility sales volume spreads out the utility's fixed cost, thus reducing their costs for gas.

At a procedural level, the utility argued that AGL&G did not have proof of injury and, therefore, lacked standing. Moreover, the Commission did not have the authority to substitute its judgment for that of the utility's management in making business decisions.

4.2.3 Decision

On July 8, 1983, the Commission dismissed the complaint without a hearing. It stated that:

1 Alagasco now indicates that it was not required to disclose this data, pending the disposition of its motion to dismiss the complaint.

2 It should be noted that Alagasco compared its price to that of AGL&G's sale price. The retail price is approximately $20 higher than the utility's.
such a merchandising program is not subject to the jurisdiction of this Commission, except to the extent the accounting practices of the utility must be in conformance with the Uniform System of Accounts...

It ordered periodic audits to be conducted to ensure compliance with the Uniform System of Accounts.

4.2.4 Conclusions

The explanation of the dismissal of this case by the PSC without a hearing is unclear. The PSC claimed that it had no jurisdiction, except over the issue of proper accounting under the Uniform System of Accounts. This was exactly the issue raised by AGL&G, nevertheless the case was dismissed. The PSC did indicate, however, that it would review the accounting procedures employed in this program in future proceedings. The supplier contends that the utility offered to buy the grills it was marketing from AGL&G. The supplier felt that his only option was to accept the utility's offer. Apparently the dismissal of the complaint was related to this arrangement. The utility disputes this, however, indicating that it decided three months later to acquire a second gas grill line from another manufacturer. After that decision was made, Alagasco was informed that AGL&G was the manufacturer's distributor in its service area. Thus, the utility contends that the complaint dismissal is unrelated to the arrangement with the utility.

This case highlights a couple of the difficulties that an individual contractor can face when attempting to bring a complaint against a utility for unfair competition. First, without raising the complaint as a rate intervention, the contractor cannot easily gain access to utility books or records because these are frequently considered proprietary information. It is therefore practically impossible to determine if a utility is charging a fair and reasonable rate for its services and products and is not funding any of the non-regulated activities from its ratebase. In the Alagasco case, the contractor felt he would have had more success with a rate inter-

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1 The administrative judge in charge of the case was not available for comment, and thus it could not be confirmed that AGL&G's arrangement with Alagasco actually led to the dismissal of the case, and thus was actually a form of settlement.
vention, but he could not wait for this to happen. The utility has not filed a rate increase for several years, other than to meet increases in the cost of its gas supplies. The contractor was also advised by his attorneys that the latter would not be an effective forum in which to raise an objection to other utility tariffs.

Second, the financial burden on a single contractor to bring a complaint of unfair utility competition is very high. Even if a contractor is able to bring the complaint before a PUC, the economic burden of the process necessitated that the contractor consider seriously any utility offers to settle, which appears to have been the case with AGL&G.

4.3 NORTHWEST NATURAL GAS

The Northwest Climate Conditioning Association (NCCA) filed an initial complaint with the Oregon Public Utility Commissioner (PUC) on September 12, 1979 opposing Northwest Natural Gas' (NNG) free and below-cost customer appliance services. Subsequently, NCCA commenced a civil suit against Northwest alleging the same matters and their anti-trust implications. The civil suit was suspended pending the ultimate outcome of the complaint before the Commissioner. A second complaint was filed by NCCA on January 15, 1982 alleging predatory practices by Northwest against NCCA members. NCCA generally argued that NNG had not properly allocated the costs of providing these services and had systematically excluded NCCA members from business referrals. The Commissioner consolidated the two complaints for hearing and rendered his decision on February 22, 1983. The decision was appealed and on May 16, 1984 the Multnomah County Circuit Court entered its decision on appeal. NCCA appealed the Court's decision on inspection, adjustment and pilot light relighting service, and Northwest cross-appealed the Court's decision on the issue of tariffing requirements for repair activities. On January 29, 1986, the Oregon Court of Appeals remanded the case to Multnomah County on technical grounds without reaching the issues raised on appeal.

4.3.1 Legal Jurisdiction

Although, this complaint was not brought as a rate intervention, the Commissioner could address the complaint under ORS 756.300, a general

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provision for addressing complaints. In fact, according to ORS 756.040(1), as noted by the NCCA, it is the Commissioner's duty to protect customers "from unjust and unreasonable exactions and practices and to obtain for them adequate service at fair and reasonable rates."

4.3.2 Description of Case

Complainants

NCCA and its members raised four basic issues before the Commissioner and the Circuit Court. Only one of the issues, regarding customer cost of receiving inspection and adjustment services, was subsequently brought before the Appeals Court.

One of the primary complaints raised by NCCA concerned NNG's policy of charging the cost of inspection, adjustment, repair and replacement services on customer-owned appliances to the utility's natural gas rates (e.g. expenses). For example, NCCA noted that in 1980 the utility conducted 37,969 free service calls. Even for thermocouple replacements which were charged directly to the customer, according to NCCA, NNG based the cost on an allocation of 15 minutes per service charge, and did not include travel time or overhead. NCCA argued that these services should not be charged to the ratepayers because they are non-regulated activities; charging for services in the natural gas rates without actually rendering them is illegal; and the practice results in unfair discrimination and unfair burden between customers who use the service and those who do not.

In addition to charging appliance services costs to the ratepayers, NCCA also charged NNG with not filing separate tariffs for required services (i.e., pilot light relighting, inspection and adjustment), and for filing no tariff on certain direct charges that were made to customers. According to NCCA, NNG should be required "to file tariff schedules setting forth all charges levied by it for services rendered to the public, per Oregon law." The purposes of this law, ORS 757.205, are to provide both the PUC and utility customers with the opportunity to review the utility's accounts, to protect consumers, and to prevent discrimination and cross-subsidization.

A third major issue raised by NCCA concerned the utility's policy of referring customer requests for service to contractors selected by the utility. NCCA claimed that it is illegal for the utility to refer potential customers
for natural gas appliances to a select group of firms, and that the referral practice was deceptive because it leads customers to believe that they are being referred to the best dealers or repairmen. Furthermore, the complainant argued that the utility systematically excluded members of NCCA from receiving referrals. The utility also obtained favors from the contractors which received customer referrals, according to the NCCA.

A fourth issue centers on the NCCA's charge that NNG is attempting to extend monopoly control over the gas appliances repair and sales business by cross-subsidizing and bundling services on appliances. NCCA points out that the bundling of services was one of the major reasons why AT&T was required to divest its service and repair operations.

A final issue arose after the initial complaint to the Commissioner was made. This concerned a ruling which amended OAR 860-21-010, a regulation which, in its initial form, required the utility to provide customer assistance in securing efficient service and to "render every reasonable assistance to enable the customer to secure appliances properly adapted and adjusted to the service furnished." The amended ruling required the utility, upon customer request, to "inspect and adjust customer-owned appliances and facilities for safe and efficient operation." The NCCA charged that this new rule would give the utility virtual monopoly control over the appliance repair business, and furthermore, that the amended rule was at variance with the established policy that the utility has no responsibility for customer gas appliances. NCCA also argued that the Commission violated specific rulemaking procedures in amending the rule. These violations included improper notification of the proposed amendment and misleading information on the nature of the amendment, which did not allow interested parties an opportunity to present opposing views and arguments. The Commissioner had described the rule change merely as a "housekeeping" matter.

Utility

NNG presented several arguments in support of retaining its customer appliance services, and refuting NCCA's claims of unfair discrimination in the utility's referral system.

In defense of its customer services, NNG argued that, first of all, customers are not being charged for the service itself, but for the availability of that service. In other words, ratepayers are sharing equally in
the cost of a service which is equally available to all customers at no
direct charge. Secondly, the utility argued that the inspection, adjustment
and relighting services were "utility services" for which no separate
tariffs need be filed. Finally, sale of merchandise is not a service in any
sense, and therefore does not require a separate tariff to be filed.
According to NCCA, however, Oregon law states "Service is used in its most
broadest [sic] and most inclusive sense and includes equipment and facilities
related to providing the service or the product served." [ORS 756.010(11)]

NCCA states that there is no functional difference between services for
which there is a charge and those for which there is none.

The utility's arguments for providing the referral service rely on its
legal obligation and the public interest. NNG points to OAR 860-21-010,
described above, in support of its contention that it has an obligation to
furnish the services. These services are important to the public interest
because they promote safety and conservation. Furthermore, if customers
were charged for the services directly, they may be tempted to forego an
important inspection or repair. NNG disputes NCCA's claim that its referral
service is misleading and discriminatory by stating that it refers contrac-
tors on technical criteria and on the basis of who it thinks "will present
natural gas in a favorable light..." The utility argues that it has the
right to make referrals to firms that it believes are more likely to promote
gas sales.

4.3.3 Decisions

Because this case has been taken to the level of the Oregon State
Court of Appeals, there have been two sets of decisions, with one more
decision still pending from the Appeals Court. The points covered by the
Commissioner and the trial court are discussed together, followed by a
brief description of the arguments presented in the appeal.

Public Utility Commissioner of Oregon and The Circuit Court of the
State of Oregon for the County of Multnomah

In its decision, entered on February 22, 1983, regarding the authority
of the utility to charge the costs of its customer services to the rate
base, the Commissioner drew a distinction between appliance repair services
and inspection, adjustment, and pilot light relighting services. In the
first area, the Commissioner found that appliance repair services are a non-utility function for which costs must be fully recovered from the customers receiving the services. The trial court, in its May 16, 1984 decision, upheld the Commissioner's decision.

In the area of inspection, adjustment, and pilot light relighting services, the Commissioner found that these activities are important safety and conservation services which may be expensed, although a separate tariff must be filed. The trial court fully upheld the Commissioner's decision.

The Commissioner found that the utility's referral policy does serve a valuable public service. It found the complainants' suggestion that customers rely on the phone directory and their own intuition in identifying and judging the quality of potential contractors to be ineffective. Furthermore, it denied NCCA's claim that the utility had retaliated against its members or had accepted favors from other contractors because the Commissioner found that the complainant had not met its burden of proof. The trial court upheld the Commissioner's decision, stating that he could not substitute his own judgment for that of the Commissioner's in this case.¹

Independently, the circuit court made a distinction between the utility's appliance services and its merchandising program (i.e., sale of gas ranges, ovens, dryers, barbecues, and lights). It remanded the matter to the commissioner to determine whether a separate tariff was required for these activities.

The issue of whether the Commissioner had acted properly in proposing and making amendments to OAR 860-21-010, allowing utilities to inspect and adjust appliances, was examined and acted on by the trial court. The latter found that the procedures used by the Commission in changing the rule were not valid. The Commissioner had not properly informed interested parties by stating that the amendment was merely a housekeeping matter. On the contrary, the court found that the change had a significant impact on the obligations of the utility.

¹ The utility had changed its policy regarding referrals before the commissioner's decision to require any business requesting referrals to show that it has proper state and local licenses and, for contractors installing water heaters, to show that the supervising plumber on a project is also licensed.
In bringing its case before the Appeals Court, the NCCA appealed only the ruling on the utility's inspection, adjustment, and relighting services. It based this appeal, first, on Oregon law, which, it alleged, requires that services be charged separately, and secondly, on the argument that the safety and conservation claim was not supported by substantial evidence.

The Commissioner, as defendant in the case, claims that the NCCA did not meet its burden of proof regarding the above services, and that the Commissioner reached his decision in an appropriate fashion. The Commissioner stated that the service does advance safety and conservation while not significantly increasing the price of gas to customers whether they use the service or not. A separate charge would also inhibit customers from requesting the service when they need it. Finally, no state statute requires that a separate charge be levied.

HNG entered the appeals case as intervenor-respondent and cross appellant. It supports the Commissioner's basic arguments presented above, and adds that NCCA's complaint is purely a matter of ratemaking, in which the Commissioner has wide discretion. As cross appellant, HNG is appealing the court order requiring the utility to file separate tariffs for its repair and replacement activities.

4.3.4 Conclusions

The NCCA was effective in one important area, that of requiring the utility to file separate tariffs for some of its service activities. The filing of separate tariffs will enable them to monitor closely the utility's service activities to ensure that no cross-subsidization occurs. However, NCCA did not prevail on the issue of free inspection and adjustment service.

The NCCA was also successful in having the Commissioner order a cost and revenue separation study, which was filed by HNG within 60 days. No comments were received on the study. According to HNG counsel, the study showed that the thermocouple repair and replacement activity was appropriately allocated. No study of the sales activities were prepared, although the order addresses the "unregulated operations, including repair and sales program." Further, the Commissioner ordered that the gas appliance maintenance program be fully supported by the gas appliance sales program.
4.4 CONNECTICUT NATURAL GAS

A detailed analysis of all the proceedings in this case is beyond the scope of the present report. However, the basic complaints against Connecticut Gas remained generally constant throughout, although a variety of different legal approaches were attempted. The present analysis will focus on two representative areas:

- A summary of the issues brought before the Connecticut Public Utility Control Authority (PUCA) during the rate hearings, and the relevant decisions; and
- A summary of the basic arguments and decisions in the 1976-81 complaint before the District Court, Joseph Paquette, D.J. DeMaio and Les Dempsey (plaintiffs) vs. Connecticut Natural Gas Corporation (defendant).

4.4.1 Legal Jurisdiction

The action was instituted in the District Court under 15 U.S.C. secs. 4, 15 and 26 and 28 U.S.C. sec. 1337 "to prevent and restrain and to award damages for the continuing violation by the defendants [CNG] of Secs. 1 and 2 of the Sherman Act, as amended, 15 U.S.C. Secs. 1 and 2... This Court has jurisdiction under the Clayton Act."

Mr. Joseph Paquette, a Hartford, Connecticut contractor, has pursued a number of different actions against Connecticut Natural Gas (CNG), in several different jurisdictions, over a period of years. Between 1976 and 1983, for example, Mr. Paquette participated as an intervenor in four separate rate hearings before the PUCA; was involved in extensive and protracted litigation comprising several different actions before the U.S. District Court of Connecticut, where he charged CNG with restraint of trade; and appealed a PUCA finding before the Superior Court of Connecticut.

4.4.2 Description of Case

Over the years, Mr. Paquette, Mr. DeMaio and Mr. Dempsey (referred to in the present analysis as the plaintiffs), took two basic tacks against CNG: first, before the PUCA, Paquette sought to show that CNG was improperly allocating costs for its unregulated merchandising and jobbing (M & J) activities, so that those costs were being unfairly subsidized from the
ratebase; and second, before the courts, they argued that CNG's merchandising and jobbing activities worked to fix prices, compete unfairly with independent contractors, and to illegally favor selected contractors.

Rate Hearings Before the PUCA

Mr. Paquette's position before the PUCA during this period was that the field of appliance sales and service is not essential to CNG's regulated delivery of gas. He presented testimony, particularly during the 1980-81 hearings, that the utility's M & J activities were a marginal profit or loss area and therefore should not be subsidized by the ratepayers. (The M & J activity was at that time an above-the-line activity, a very atypical designation by the PUCA.) He asked that rate increases not be granted to CNG until it removed itself from the appliance sales and service field, or relegated those activities to areas not subsidized by the gas consumer.

During the 1979-80 hearings in particular, the plaintiffs claimed that several specific areas of subsidy and improper allocation had been identified. The three principal areas of concern were the following, according to the plaintiffs:

1. CNG failed to properly account for its merchandising and jobbing activities (primarily the sales and installation of appliances). For example:
   - No advertising expenses had been charged to the merchandising and jobbing accounts;
   - No costs were allocated for parts of the CNG headquarters building apparently used for the display of appliances, and a partial allocation for other CNG building space used for merchandising activities;
   - Some percentage of commissions paid to CNG "energy consultants" could be attributed to the sale of gas appliances, and were not allocated to the merchandising accounts;
   - An insufficient amount of CNG's annual phone bill had been attributed to the merchandising accounts;
   - The labor costs for certain marketing and advertising activities were not reported in the merchandising accounts.

2. The merchandising and jobbing activities of CNG, even without fully allocated costs, showed profitability of much less than system average. The total admitted cost of Account 915 (entitled "Cost of Merchandising,
Jobbing and Contract Work”) in the rate hearings test year had been $1,058,859, while the admitted income had been $1,170,907, a claimed profit of about 9.56 percent. CNG testified that the further increases in charges that would be necessary to increase the profit would result in the utility charging substantially more than most contractors, resulting in "adverse consequences on the company’s overall efforts for gas load retention." Mr. Paquette argued that if, by the utility's own admission, it could not maintain its merchandising and jobbing activities at system average return, and the services were readily available to consumers through non-regulated businesses, then the utility's activities in that area were unnecessary and should be discontinued.

3. CNG failed to separately account for revenues and expenses from its Residential Gas Heat Service Plan (providing customers with a year's maintenance and parts replacement for $29.00 per year).

CNG did not respond in 1980 to the specific allegations of cross-subsidy. It did indicate its opposition to making the program a below-the-line activity.

Case Before the District Court

Although, as noted above, the plaintiffs argued a number of different actions before the Court over approximately a five-year period, most were connected with a single civil complaint filed in 1976 charging that CNG, as a monopoly, pursued a deliberate policy of unfair competition in the appliance sales and service area.

Two arguments were central:

- CNG forced independent plumbing and heating contractors out of business, not only by its own activities in that area, but by establishing an "approved list" of contractors for the installation and maintenance of gas water heaters and heating systems, fixing the prices they could charge, and coercing CNG customers into accepting service only from them. These actions resulted in restraint of competition, and increased barriers to entry into the market for selling, servicing and maintaining these heating systems.

- CNG’s Residential Gas Service Plan constituted an illegal "tying" arrangement, in violation of the Sherman Act. The plaintiffs
contended that this plan was provided through CNG's regular facilities and costs for administering it were included in CNG's charges to its gas customers. The plaintiffs argued further that because independent contractors lack the economic power CNG derives from its public utility status, they are at a substantial competitive disadvantage. CNG denied the substance of the plaintiffs' claims.

4.4.3 Decisions

Before the PUCA

On June 25, 1980, the Connecticut PUCA found that "the Company's (CNG) merchandising and jobbing activities are being subsidized by other ratepayers and this subsidization should be eliminated."

The PUCA ordered that CNG make a study of all joint and common costs properly attributable to the Company and one or more of its subsidiaries. Upon completion of the study, but no later than six months from the date of the decision, CNG was ordered to provide the PUCA with (1) a written description of each category of such "common" cost; (2) the procedures utilized to allocate these costs, and (3) the rationale underlying the allocation procedures.

The PUCA directed that merchandising and jobbing activities should be excluded from rate base and expense items, and that future cost-of-service items should contain information on merchandising and jobbing sufficient to verify allocation of joint rate base and expense items.

A comprehensive allocation study was published by CNG in November, 1980. CNG attempted to identify all joint and common costs. Four specific areas of concern had been raised in the PUCA directive to undertake the study: Facilities Costs; Information Systems Expenses; Other Employee Benefits; and General Legal and Accounting Expenses. For each area, CNG explained the manner in which costs were incurred, and proposed a rationale for future allocations. This treatment was extended to other major areas of shared costs, such as staff payroll, corporate insurance, and customer service trucks, as well as to less obvious items such as display area, employee welfare expenses, and postage. Nevertheless, after the 1983 rate
hearings, the PUCA found that "the Company's allocation procedures fail to apportion to subsidiaries their proper share of joint and common costs. Use of the Massachusetts Formula is reasonable for this case." Of particular concern to PUCA staff was the allocation of executive salaries, and the pricing of services rendered by the parent to subsidiaries and by subsidiaries to the parent.

The PUCA directed that, after completion of the staff audit of the Company's study of joint and common costs, a meeting of staff and "interested parties" should be held to discuss differences, followed by a hearing, if necessary. It was stated in the PUCA's directives that "[p]rovisions of services to the rate base utility by a non-regulated affiliate must be at cost. Provision of services by a regulated utility to a non-regulated affiliate must be at reasonable charges." Further, the PUCA ordered that, if bill inserts, mailings, or other solicitations of Company customers are to be used to promote a below-the-line or unregulated activity, the PUCA should be notified and a method of determining the value of this service should be developed, filed and approved by the PUCA before such mailing or solicitation occur.

In January, 1984, CNG submitted an updated inter-company transaction review, incorporating recommendations from the PUCA staff audit, as well as PUCA findings in prior rate proceedings concerning the identification and treatment of joint and common costs. The estimated financial impact of the revised procedures amounted, according to the new review, to an additional annual charge to the company's non-regulated operations of approximately $122,600. According to CNG, no more that $20,000 of this is attributed to M & J activities. For the test year 1979, for example, this would have added nearly 12% to merchandising and jobbing costs of $1,058,859. The new charges ranged in scope from employee benefits to charges for office space, outside service fees, and general corporate expenses.

According to the 1984 report, CNG believed that all major concerns previously raised by the PUCA had been effectively addressed and "hopefully resolved" by the completion of the new review, and the implementation of identified changes.
Before the District Court

All of the plaintiff's actions against CNG were eventually dismissed. Several pleas were denied on technical grounds -- for example, the Court denied the plaintiffs' qualifications to represent a "class" for a class action, and there was some question as to the statute of limitations on some of the plaintiffs' complaints -- and some were denied for a simple lack of proof as to the plaintiffs' allegations against CNG.

The Court's ruling on one of the actions, on July 7, 1977 -- a request for a preliminary injunction against CNG -- outlines the Court's basic findings. The Court found that the Residential Gas Service Plan was "purely optional" to home heating customers, and that the plaintiffs had been unable to show that CNG had used its monopoly position in the gas supply market to "foist" those services on unwilling customers. Further, the Court did not recognize the existence of an improper subsidy giving CNG an unfair competitive advantage in the repair and maintenance market. The Court expressed the opinion that, following the command of the PUCA, CNG "maintains scrupulously separate accounts for expenses of the service plan." Labor, parts, billing machinery, storage space, even the allocable costs of the tools used by the workers when making service calls were all debited from the service plan account. The Court had no reason, based on the facts presented, to suspect that CNG's records were false, or that it was, in effect, "duping" the PUCA.

Regarding the allegation that CNG was engaging in predatory pricing, and so attempting to monopolize the market for repair and maintenance of gas heaters, the Court stated in its decision that CNG made a substantial profit on those contracts of some $9.00 per customer, and that thus the Court concluded that price greatly exceeded average cost. The Court could find nothing to make it suspect the legality of the service contracts.

In an earlier decision, the Court had found no basis for the plaintiffs' claim that they had suffered any damage from CNG's alleged "conspiracy" with other contractors, or, in fact, that such a conspiracy existed.

The net effect of the small business interventions in CNG's rate-making cases was substantial. Most importantly, the costs of merchandising and jobbing (M&J) activities, those in direct competition with independent contractors, were removed from the utility's rate base. As long as the M&J
accounts were "above the line," the guaranteed rate of return that CNG could earn from these activities constituted an unwarranted incentive for their expansion beyond what might be argued to be economically efficient.

Once these activities have been accounted for separately from the provision of the utility service proper, the scrupulous allocation of costs between the regulated and unregulated activities allows contractors, the PUCA, and the utility itself to assure that cross-subsidization has been eliminated and that predatory pricing does not occur.

4.5 WISCONSIN POWER AND LIGHT COMPANY

4.5.1 Legal Jurisdiction

The complaint, alleging that Wisconsin Power and Light Company (WPL), an electric and gas utility, was subsidizing its activities in the mechanical trades, was heard before the Wisconsin Public Service Commission (PSC) in 1983.

In 1982, the Allied Mechanical Employers Council (Allied), had intervened before the PSC in WPL's regular rate request proceeding. To support its assertions of unfair competition and cross-subsidization, Allied hired an independent consultant (Technical Associates, Inc.), which also prepared testimony in support of the small businesses in the Minnegasco and Northwest Natural Gas proceedings cited earlier, to analyze in detail the utility's accounting system as it related to the way costs were allocated for "customer servicing activities," primarily the sales, installation, repair and maintenance of appliances and equipment. Based in part on Allied's resulting critique, PSC staff also examined the utility's customer servicing practices.

In the course of the PSC staff audit, significant downward adjustments were made in the company's revenue requirement, and shortly afterward, the utility dismissed its rate increase application. But at Allied's request, the customer servicing issues were split off into a separate formal complaint before the PSC.
4.5.2 Description of Case

Allied, a trade association made up of contractors (primarily small businesses) in the heating, air conditioning, plumbing and other trades, objected to WPL's increasing involvement in customer sales and servicing for two basic reasons. One, Allied felt that since independent contractors were unable to provide similar services at rates as low as those offered by the utility, it was likely that unregulated activities were being subsidized by the regulated ratebase. Two, Allied was concerned that the utility enjoyed an unfair competitive advantage over small heating and plumbing contractors.

In the original rate-increase hearing, Allied voiced a number of general complaints:

- The utility's activities, especially in the area of service and installation of conversion burners, new furnaces and energy conservation devices, were in direct competition with independent contractors;
- The utility could access credit records for virtually every citizen in the service area;
- The name recognition of WP&L extended beneficially to its non-regulated activities;
- The utility had access to extensive social and economic data unavailable to a small business; and
- The utility was using its mailing lists and regulated billing mechanisms to advertise and in some cases bill for unregulated services.

In addition, Technical Associates testified at the rate hearing that its analysis indicated that the utility's policies and practices served to overcharge customers for regulated service and undercharge customers for unregulated service by as much as $569,000 per year, compared to total operation and maintenance costs of $10,194,172 in 1981. Although that estimate was not offered as precise, Technical Associates' report concluded that

"customers who partake of the Company's (WPL) gas distribution services are being required to bear a substantial amount of cost for which they are not responsible."

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As noted above, WPL later withdrew its rate increase request. Also, the utility made a number of changes in its customer servicing activities (see Decisions section below), the major one being the establishment of comprehensive new accounting procedures for the stricter allocation of costs between regulated and non-regulated activities. However, Allied considered several serious questions to be unresolved, despite the changes, and the PSC agreed to a new complaint proceeding.

WPL's specific unregulated activities in question in this case included:
- Appliance repairs (WPL repaired such appliances as microwaves, dehumidifiers, washers, dryers, ranges, refrigerators and air conditioners);
- The "Security Blanket" program (a furnace inspection and warranty plan);
- Sales and installation of furnaces, plenum heaters, electronic ignition devices and automatic vent dampers;
- Sales of appliances to employees (those mentioned above, as well as refrigerators, freezers, water heaters and computers);
- Warranty service on customer appliances;
- Various service work on gas and electric installations, such as adjustments, relighting of pilots, replacements of fuses and conversions from LP to natural gas.

A distinction was made between "above-the-line" and "below-the-line" activities. Included within the definition of "above-the-line" activities, or those related to the utility's distribution and delivery of gas and electricity, were such non-billed activities as investigation of gas odor, no pilot, etc., and such billed activities as repairing customer-owned appliances and selling flue dampers and intermittent ignition devices. Although such customer installation activities are, strictly speaking, unregulated (there are no Commission-approved tariffs or rate schedules governing that business), the PSC still regards them as above-the-line, since they result in revenues that reduce WPL's cost of service for rate making purposes, while related expenses increase the cost of service.

Functions such as appliance warranty services, the Security Blanket program, and the sale of furnaces and plenum heaters were considered "below-the-line," and therefore, neither the revenues nor the costs from this
merchandising, jobbing and contract work should have affected the revenue requirement of gas distribution service. WPL maintained that the revenues and expenses for below-the-line activities were properly accounted for and, therefore, were not subsidized by ratepayers.

At the pre-hearing conference, five issues were formally identified. The transcript lists these issues as:

1. Was WPL properly accounting for customer sales, service and repair activities? Sub-issue: To what extent were those activities required?
2. Did subsidies exist above- or below-the-line for those activities?
3. Should those activities be separated functionally or legally from the regulated activities of WPL? Sub-issue: Should any of the below-the-line activities be above-the-line because of their effect on the public interest?
4. Does the utility enjoy unfair competitive advantage from the comingling of regulated and unregulated activities? (It is important to note that this issue was established as "incidental" for the purposes of the hearing. According to the pre-hearing conference report, "[m]aterial on [this issue] within reason would be allowed into the record if it flowed out of the other material, but it was not going to be a major piece of the case with major amounts of affirmative testimony.")
5. Whether the PSC should establish a cost justified rate for above-the-line activities, and what activities should and should not be charged.

Allied's principle arguments centered around three basic positions:

- That, as a monopoly, the utility enjoyed advantages that represented unfair competition to private businesses;
- That even the new accounting system did not sufficiently safeguard against improper cost allocations and resulting cross-subsidization; and
- That the utility offered a number of free services that went beyond those required for the public interest, thus discouraging the use of private contractors, and causing ratepayers in general to subsidize services performed for individuals.
Allied charged that the utility’s enormous financial power, access to credit records and other social and economic data, name recognition, purchasing power and economies of scale, and use of lists and audit information for advertising and marketing, were all derived from its status as a regulated monopoly, and gave it advantages no private contractor could hope to match. Allied tried to demonstrate that most of the sales and services which WPL offered -- all but activities such as checking gas leaks and other "before the meter" services that only utility personnel were allowed to perform -- were readily available from independent contractors. Allied’s executive vice president testified that there was 26 percent unemployment in the labor pool drawn on by contractors in the general service area, and even WPL witnesses agreed that the utility was not offering these services because it perceived any lack of qualified contractors.

WPL, on the other hand, pointed out that Allied witnesses did not know how many furnaces or heaters had been sold (the utility submitted that only about 50 had been sold in the past two years), could not cite any specific instances of how WPL’s credit records had been used, or of WPL billing customers for appliances in their regular utility bills, and had no knowledge of any Allied members attempting to make use of the Advance Plans (containing social and economic data and forecasts) regularly filed by the utility. As to the monopoly/unfair competition argument in general, WPL considered the issue tangential, and did not argue it extensively, citing the pre-hearing conference agreement that it was not to be considered a primary issue.

The new accounting system, however, received intensive attention during the complaint testimony, and was scrutinized in close detail. Although the witnesses, including the Allied experts and PSC staff auditors, seemed to agree that the system was generally designed to allocate costs between the regulated and unregulated activities "fairly and reasonably," Allied had several specific concerns: that upper and mid-level utility management time was not charged to unregulated activities; that travel time to service calls where both billed and unbilled service was performed was not charged to the customer; that the new accounting system was not applied to the employee merchandise program; and that certain joint overhead costs (such as buildings and labor) were not apportioned to unregulated activities.
Allied also had an overall concern that, since it was up to the utility to decide which calls were billed and which were not, and how the costs should be allocated, the potential for subsidy, even inadvertent, would always exist, since no outsider, not even the PSC, could hope to monitor all such detailed allocations. An expert testifying for Allied observed that substantial cross-subsidization could arise because "the company [WPL] did not charge for the large majority of service calls ... and because the comingling of regulated and unregulated activities provided the company with the opportunity to improperly attribute costs to [installation, repair and merchandising business]." Allied concluded that the only possible way to prevent cross-subsidization was to make the unregulated activities a wholly separate subsidiary.

WPL countered that the amount of time upper level management spent on unregulated activities was negligible, and none had been demonstrated. Further, although conceivably a subsidy, the travel time and joint overhead costs in question were small amounts that did not justify the expense of additional accounting procedures, and were proper costs of doing regulated utility business. WPL presented evidence that the majority of their nonbilled gas service calls for the past three years (87 percent, 98.6 percent, and 96.6 percent in 1980, '81, and '82 respectively) were in response to gas complaints. Although a very small number actually resulted in the detection of gas leaks, the utility argued that it would not be adequately discharging its legal responsibility for the safe and efficient distribution of gas if it discouraged customers from calling about such conditions as suspected gas odors, faulty pilot lights, no heat, or high bills. WPL held that it was fair for ratepayers to bear the cost of such activity because leaks, problems in pressure or on the line, and other "utility-related" problems could impact not only the individual customer, but the quality and safety of gas service to other ratepayers.

4.5.3 Decisions

On September 6, 1983, the PSC dismissed Allied's complaint. The letter informing Allied's counsel of the decision offered the following reasons:

1. Since WPL had amended its accounting practices for non-utility services, its current practices were deemed adequate to maintain
2. No subsidization of non-utility services by ratepayers had been shown to the commission's satisfaction.

3. The record did not support the necessity for the formation of a separate subsidiary to perform non-utility services.

4. Significant safety concerns militated against forcing the utility to contract these customer services out to other providers.

Since the PSC made no further explanation, their precise reasoning can only be speculated upon. However, a few issues can be observed. The PSC clearly considered the issue of a monopoly's unfair competition in the marketplace to be peripheral, at best. Allied's arguments -- many citing the AT&T case -- outlining the potential for abuse, seemed to be outweighed by the fact that no actual, current instances of abuse could be demonstrated to the PSC's satisfaction. The new accounting system, and the general agreement on its soundness, were considered adequate safeguards against improper cross-subsidization. And the question of safety and other public responsibilities of a utility seemed to be a compelling issue, with the PSC inclined to give WPL the "benefit of the doubt" in such matters.

Although the formal complaint was dismissed, it is important to note the changes that followed the initial intervention before the rate hearing.

1. The utility completely revised its accounting procedures with respect to allocating costs to customer sales and service activities. A number of cost items which Allied had identified as non-allocated and which were accounted for in the new system were:
   - Building space;
   - Computer usage;
   - Furniture and equipment;
   - Communication costs;
   - Tool costs;
   - Employee pensions, benefits and taxes related to direct labor dollars; and
   - Return on investment after tax related material costs.

2. The utility increased the annual charges for its Security Blanket program from $59.95 to $79.95
3. The utility increased its standard billing rate for service and repair of customer equipment.
4. The utility stopped including Security Blanket advertising in its customer billings.

Although it is difficult to assess the exact extent to which these and other perceived changes in the utility's involvement in customer sales and servicing can be attributed to Allied's actions, they should be evaluated as a significant element in the overall case.

The overhaul of WPL's accounting system to properly allocate costs to customer sales and service activities constituted a major improvement over the situation that had existed before Allied's intervention. Moreover, the careful scrutiny by the PUC to assure the proper placement of accounts above and below the line served to further equalize competition between the utility and independent contractors by removing non-regulated activities from the rate base. It should be added, however, that the cost of this intervention created a substantial hardship on Allied's operation.

Allied was less than fully satisfied, however, since the accounting system, however well-designed, relied upon a myriad of subjective utility decisions to assign particular costs to the proper accounts. Since these decisions cannot be adequately monitored, Allied felt that the possibility of substantial cross-subsidization remained. These concerns have been allayed, apparently, by the recent Wisconsin legislation that requires that utilities wishing to engage in non-utility activities form a holding company in which utility and non-utility activities are carried out by separate subsidiaries. (See Section 2.5.2 State Legislation.)
5.0 CONCLUSIONS AND RECOMMENDATIONS

5.1 Conclusions
The preceding analysis of actions brought against utilities by small businesses and their trade associations that seek redress for utility anti-competitive behavior provides the basis for several conclusions.

1) The only predictably effective forum under existing law in which to raise cross-subsidization issues is the state Public Utility Commission (PUC). The issues are best raised in rate hearings with the intervenor alleging unwarranted subsidy by rate-payers of non-regulated activities;

2) The successful resolution of such complaints hinges upon the equitable allocation of costs and revenues between regulated (above-the-line) and unregulated (below-the-line) activities;

3) Actions alleging anti-competitive behavior by the utility apart from rate-payer considerations are unlikely to be sympathetically heard by PUCs; and

4) Suits brought before the federal courts are costly and unlikely to be successful. The FTC does not appear to be interested in supporting the antitrust claims of small businesses.

5) State legislation, with few exceptions, does not directly address the utility competition issue.

Of the five key cases analyzed, four resulted in significant changes in utility behavior likely to make small businesses more competitive. All five were brought before PUCs. Of the four successful actions, three were brought in rate-making hearings. In all five of the actions, the resolutions hinged on cost allocation changes ordered or accepted by the PUC. In the cases of CNG and Wisconsin Power and Light, detailed accounting reviews were undertaken. In the Minnegasco and Northwest cases re-allocations were ordered. Even in the Alabama case, in which the complaint was dismissed without a hearing, the PUC cited the utility's adherence to the Uniform System of Accounts prescribed by the National Association of Regulatory Utility Commissioners (NARUC).

The initial distinction that the Alabama Public Service Commission failed to make was between accounts and allocations to those accounts. As promulgated by NARUC, the Uniform System of Accounts has accounts for the provision of utility services.
goods and services beyond the meter: Merchandising (Goods) and Jobbing (Services) (M & J). The system is, however, silent on the allocation of common costs between regulated and M & J activities. And, as we have seen, this is the critical issue.

Even if an allocation methodology was to be included in the Uniform System of Accounts, as they stand, affiliate transactions would not be segregated from utility transactions. Although any merchandising or jobbing activities would then show up in the M & J accounts, there would be no way to distinguish between activities of discrete affiliates.

It should be noted that in two of the unsuccessful cross-subsidy cases brought before the PUCs, Inter-Mountain and LaClede I, intervenors raised the issue of utility service costs vis-a-vis fair competition rather than rate-payer subsidy. In both cases the PUCs determined that the intervenors had failed to demonstrate their allegations. It is certainly possible that had the intervenors in these cases sought to demonstrate that the utility practices in question resulted in rate-payer subsidies of those practices, that adequate records could have been adduced to resolve the issues.

Finally, only one intervenor was successful in using the federal courts for redress under the Sherman or Clayton Anti-trust Acts; nor are future efforts in this direction likely to be more successful. This is true for a variety of reasons:

1. Such proceedings are prohibitively expensive for a small business and even for many trade associations;
2. The burden of proof is on the plaintiff to demonstrate predatory pricing practices, as opposed to the situation in rate-making hearings where the utility must justify its expenses in the face of challenges;
3. The barriers to entry in the contracting business have been held to be too low to support allegations of a utility's forcing competitors out in order to gain control of the market; and
4. Finally, if pending Administration proposals are accepted by Congress, treble damages will no longer be awarded for Clayton or Sherman Act violations. The incentive for bringing such cases to the courts will be reduced even further.
5.2 Recommendations

Small business advocates can conceivably have a significant impact in protecting small businesses from anti-competitive behavior by utilities by working with such organizations as the National Association of Regulatory Utility Commissioners (NARUC) to promote PUC adoption of proper cost allocation procedures. Such procedures as those proposed by the Virginia Legislative Committee\(^1\) protect the interests of both rate-payers and small businesses by assuring that the costs of non-regulated activities are properly accounted for. In so doing, ratepayers are assured that they pay only for regulated services and small business is assured that non-regulated activities are fairly priced.

Where allegations of cross-subsidy are made, the adoption of an explicit allocation methodology such as that called for by the Virginia report should result in their immediate resolution. There are two reasons to suppose that small business advocates, acting in concert with NARUC in some "amicus curiae" role vis-a-vis state PUCs, could significantly protect small business interests. First, the Virginia guidelines were developed in close consultations with the utilities under the State's jurisdiction. The cooperation of the utilities stemmed from their desire to influence anticipated legislative changes in PUC legislation. Once the legislative pressure subsided, owing to change in legislative committee staff, the utilities withdrew the study from consideration. In fact, the study was theirs, and is today held under utility copyright. The utilities had found the report's recommendations to be acceptable. Given the range of interests and concerns among Washington Gas Light, Virginia Electric Power Company and Potomac Electric Power Company, one would suppose that other utilities would also find the recommendations acceptable.

The second reason to suppose that small business advocates might be successful in promoting this solution is that NARUC finds itself increasingly pressed to resolve the accounting issues posed by the increasing diversification of utilities. As of now, there is no plan on the table to deal with this issue. NARUC staff and Accounting Committee members expressed interest

in examining the Virginia recommendations as a possible solution to what is essentially an unrelated problem for them.

The adoption of the Virginia Legislative Committee recommendations or similar allocation formulas would give all interested parties the means to readily determine the costs of, and income derived from, both regulated and unregulated activities. Where a utility is cross-subsidizing unregulated activities, these formulas would make it apparent. The present study suggests that such evidence of unjustified ratepayer subsidy brought to a PUC's attention at a rate hearing will often result in decisive action by the PUC to end the subsidy.

In addition, small business advocates should also consider promotion of state legislative action to remedy the problem. Until a complaint was brought by small business groups, neither the PUCs nor utilities have apparently expended significant resources to avoid improper cross-subsidies. Therefore, pursuing better attention to accounting would bring limited results. States have two types of legislative options to supplement the above recommendation. States may decide, as in California, to restrict unregulated utility activity (no work requiring state license for over $200). Alternatively, the state could require PUCs to establish guidelines or criteria for permissible diversification activities, analogous to the NARUC Report recommendations. These criteria could be drawn in advance on a general basis, or drawn specifically for each utility venture. Also, the federal law could be amended to require that the state PUCs address the issue of utility competition and specific guidelines and criteria. This is similar to the approach of H.R. 969, which provides a forum for small business complaints at PUCs or the Federal Trade Commission.
The literature collected and reviewed for this report falls into three broad categories: utility cross-subsidization, utility diversification, and government programs and policies which can affect utility competition with small businesses. These topics are interrelated, so some overlap exists among categories. These reference materials are sorted by the above categories to assist the reader in any subsequent review.

In general, the literature review conducted for this report was extensive, but by no means all-inclusive. It did, however, suggest that only superficial discussion of utility cross-subsidization, utility diversification, and government programs and policies which can affect utility competition with small businesses has taken place. Future debate on this problem would benefit from specific in-depth analyses of the individual issues that weigh on utility competition, e.g., how costs are separated between utility and nonutility operations and whether the societal benefits of utility diversification outweigh the liabilities.

**Utility Cross-Subsidization**

For purposes of this report, the cross-subsidization topic centers on unfair utility competition with small businesses. Instances of alleged unfair competition among utilities may involve underwriting of nonutility operations (e.g., the sale and servicing of appliances) with ratepayer money. Other instances may involve the exchange of personnel or equipment between regulated utility components and nonregulated components without the payment of just compensation to the regulated utility component.

The material collected and reviewed under the topic of utility cross-subsidization comes from a variety of sources. Many of the references consist of news articles from contractor trade journals. Other references consist of government and contractor correspondence, including a 1982 Federal Trade Commission Staff "Working Paper." This document details the potential competitive difficulties imposed by the participation of utilities in the energy conservation market and suggests means to reduce the problem. The Small Business Administration's recommendations for states on utility energy-related programs, "Utility Competition with Small Businesses: Recommendations for States on Utility Energy-Related Programs and the Commercial and Apartment Conservation Service Program," is also included under this heading. This report details recommendations on how unfair utility competition with small business can be minimized. Of the materials assembled for this report, these documents provide the most comprehensive overview of the utility cross-subsidization and competition issues.


"Bylaws of Group Against Subsidized Service (GASS); A Nonprofit Corporation," No date.


Letter dated October 4, 1985 from Arthur Herold to Dennis Lavallee re: revised draft of memorandum involving jurisdiction of the FTC in utility competition questions.


Utility Diversification

This category includes all materials that relate to utility attempts to diversify into activities not directly related to energy generation and distribution, e.g., the sale and installation of weatherization measures. Utility diversification can be achieved by the formation of subsidiaries or through the creation of a parent holding company.

The source of these materials, as under the previous heading, varies considerably. Much of the materials consist of news articles from both contractor and utility trade journals. Several of the references, unlike the previous topic, are detailed analyses of the issues associated with utility diversification. One such analysis is the "1982 Report of the Ad Hoc Committee on Utility Diversification," by the National Association of Regulatory Utility Commissioners. This paper provides a comprehensive discussion of utility diversification from a regulatory perspective and provides guidance to state regulatory commissions who must examine utility diversification issues. Another important analysis of utility diversification is a scholarly paper by Malko and Enholm, "Challenges for Electric Utilities and Regulatory Commissions." This paper examines the financial problems faced by utilities that have led utility managers to pursue diversification. These two papers taken together encapsulate both the reasons why utilities seek diversification and difficulties these efforts present to state regulatory commissions and society.


Letter dated December 4, 1984 from David Flanagan, Wisconsin Department of Justice to Kevin Bromberg, U.S. Small Business Administration transmitting documents on formation of public utility holding companies.


Testimony of Allen M. Parkman Before the Utility Diversification Committee of the Legislature of the State of New Mexico, Santa Fe, New Mexico, Nov. 19, 1982.


"Pulling the Plug (Turning Off the Valve) on Utility Excursions Into the Service Business - A Special Report Prepared for Industry Contractors," Air Conditioning Contractors of America, No Date.


Note dated October 2, 1983 from Thomas Lewis, New Mexico State Senator to "Chas" transmitting testimony and miscellaneous material on utility diversification.


Sponseller, Diane, "Diversification and Holding Company Formation," Public Utilities Fortnightly, March 21, 1985, pp. 60-63


Weedall, Mike, "A Utility's Decision to Establish an Energy Services Subsidiary," Bonneville Power Administration, No date.


Government Programs and Policies

Certain Federal and State energy conservation programs have encouraged diversification of utilities into new businesses where they may compete with private contractors, i.e., provision of energy audits, supply, installation and financing of weatherization measures, etc.

Materials collected under this topic include many documents on the recently finalized Federal Commercial and Apartment Conservation Service Program (CACS) and some materials on the older Residential Conservation Service Program. The bulk of these materials consist of comments on the CACS Program and its potential effects on utility competition with private contractors. The testimony and letters submitted to the record for the February 13, 1985 hearing on the CACS Federal Standby Plan include a number of discussions of the competitive difficulties imposed on private contractors by this new Federal program.


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APPENDIX 2: STATE LEGISLATION TO CONTROL UNFAIR UTILITY COMPETITION

California


S.B. No. 1016 was signed into law by the Governor on September 14, 1984. The bill prohibits gas, heat or electrical corporations and their subsidiaries regulated as public utilities from performing work which requires a contractor's license. The law sunsets January 1, 1991.

Contacts: Steve Lehtonen 916-446-7422
Phil Vermuelen 916-920-4326

Wisconsin

- Legislation enacted in the 1985 session.

Legislation modifying the laws governing utility holding companies includes limits on the competitive practices of a system in relation to the sale, installation and maintenance of appliances which use energy supplied by a public utility affiliate.

Contact: Joan Braun 414-784-9260

Iowa


- Additional legislation proposed in 1986.

Senate File 450 was signed into law by the Governor. It requires that the Public Utility Commission shall provide small businesses with an equal opportunity to compete by providing rules that customers be provided alternative pricing proposals for energy conservation improvements.

H.F. 2236 was introduced in 1986. It limits a utility from providing construction services, materials or cross-subsidies for energy conservation improvements unless authorized by state law or permitted by the State Commerce Commission as part of a pilot program.

Contact: Dennis Hogan 515-223-6568

Illinois


House Bill 1328 was referred to the House Public Utilities Committee and a hearing was held.

1 List provided by the Alliance for Fair Competition.
Prospects for passage appear dim because the Public Utility Act is being rewritten. The bill prohibits utilities from sales, rental, installation, maintenance or repair of heating, cooling, or ventilating equipment.

Contact: Shirley Wilcoxen 217-544-3051

New Jersey

Legislation pending for the 1985 session.

The Coalition Against Unfair Utility Practices has proposed a bill which prohibits public utilities from engaging in the sale or servicing of energy-consuming products and equipment with certain exceptions.

Contact: John Spinale 609-397-8706

Michigan


The Michigan Coalition Against Unfair Utility Practices has had House Bill No. 4684 introduced with 23 co-sponsors. The bill requires utility companies to establish subsidiaries to be able to engage in home heating service.

Contacts: Sandra Miller 313-665-4681
Tony Asher 313-649-5450

Minnesota

Legislation was introduced in 1985.

S.F. 1768/H.F. 1909 was introduced to prohibit utilities from sales or service of energy-consuming products and equipment, including appliances.

Contact: Don Sullivan 612-377-4880

Oregon

Legislation was introduced in the 1985 session.

S.B. 511 was introduced and prohibits utilities from subsidizing service and repair. The bill died in the Senate.

Contact: 503-399-7344

Pennsylvania

Legislation was introduced in the House in 1985.

Following up on efforts in 1984 with H.B. 1908, a new bill (H.B. 869) has been introduced which prohibits a utility from business activities other than rendering public utility service. The bill
was referred to the Consumer Affairs Committee and hearings have been held.

Contact: Al Fruhwirth 215-435-5488

Legislation was considered in the 1983-84 session.

S. 3615 and A. 4563 were introduced in 1983 to prohibit a utility from selling and installing. The bills were not acted on.

New Mexico

Legislation was considered in the 1982 session.

House Bill 167 prohibited utilities from engaging in non-utility activity.

South Carolina

Legislation was introduced in 1985.

Dealers who sell cable dish antenna and home entertainment equipment have had H. 2939 introduced. The bill would prohibit rural electric cooperatives from selling or leasing satellite television systems or related equipment.

Contact: Gene Wilson 803-662-1447

Georgia

Legislation was introduced in 1985.

H.B. No. 639 has been introduced to prohibit electric cooperatives from selling or leasing satellite television systems and related equipment.

Mississippi

Legislation was introduced in 1986.

S.B. 2291 was introduced to prohibit utilities from sales or service of energy consuming products and equipment except through affiliated business entities which may not make use of the name, building and other utility resources.

Contact: Spence Dye 601-948-0844

Copies of the legislation are available from the Alliance:

Alliance for Fair Competition
P.O. Box 6808
Falls Church, VA 22046
703-237-8100