October 24, 1997

Tom Austin
Regulatory Assistance Project
177 Water Street
Gardiner, Maine 04345

Dear Tom,

Once again, thank you for organizing the disclosure workshops and for helping to move the discussion forward on the mechanics of restructuring electricity in New England.

Per your request, we are attaching our written comments to your final report. We appreciate the opportunity to share our perspective on some of the main issues therein.

Sincerely,

Lewis Milford, Esq. Energy Program Director
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Joe Chaisson

Written Comments of the Conservation Law Foundation on the Final Report of the New England Disclosure Project

I. Introduction

Restructuring the electricity markets presents an opportunity to achieve unprecedented reductions in air emissions in New England and throughout the U.S. From an environmental perspective, the electricity sector is currently:

•responsible for emitting 80% of the nation's acid rain-causing sulfur-dioxide;

•the largest single source of NOx (which causes smog);

•the largest single source of CO2 (a greenhouse gas that contributes to global warming);

•the largest single industrial source of toxic emissions such as mercury; and

•responsible for 50-60% of fine particulate matter in the East.

The Conservation Law Foundation (CLF) believes that establishing competitive electricity markets will produce major environmental benefits in New England. Open, competitive markets will allow new, cleaner generation to compete with existing nuclear and older, dirty fossil fueled power plants. Our analysis of regional market economics suggests that new, cleaner generation will move into the market in large volume and that this power will be cheaper than that produced by most of the region's nuclear units and

most of our older, dirty fossil units. Market activity to date is confirming our assessment: more than 6000 megawatts of new gas power plants have been proposed to serve New England, along with several new gas pipelines. We also expect to see fuel cells and many renewables begin to move into the marketplace as the multiple values provided by many of these resources can me marketed for the first time directly to customers and as the many institutional barriers that have effectively suppressed such clean technologies are removed. The impact of competition on air emissions could thus be very great as the most competitive new power plant technologies emit almost no air pollutants, when compared with emissions from New England's existing fleet. For example, if all of New England were to be powered by plants like those currently in permitting processes throughout New England, the entire region would emit only about two-thirds as much NOx and one-thirty fifth as much SO2 as is emitted today by a single 320 megawatt coal unit in New Hampshire (Merrimack II). This context should be kept in mind as we explore the value and practicality of mandatory disclosure in New England.

Our approach to analyzing any proposal (such as disclosure) that shapes restructuring is to determine whether it will help or hinder the process of encouraging the use of cleaner plants to displace dirtier ones. From this perspective, we conclude that a disclosure proposal must: (1) enhance the quality of information about electricity products, and (2) be implementable in a way that does not disrupt the potential benefits of an open market (i.e., it must be administratively feasible, not add unreasonable cost, not cause delay or confusion to the opening of competition, and be sensibly crafted so as to comply with basic legal doctrines).

II. CLF Summary Position on Disclosure

CLF is committed to finding a way that the goals of the National Association of Regulatory Utility Commissioners (NARUC) and the New England Governors' Conference. Toward that end, we have submitted our own proposal to be considered along with others in the Massachusetts legislative process. The summary points of our proposal are as follows:

1. Every retail supplier of electricity shall disclose and provide basic information about the fuel sources of its generation.

2. Retail suppliers making specific claims about electricity sources or the environmental attributes of their electricity products shall disclose the fuel sources of the generation that constitutes the products sold to its customers.

3. Retail suppliers not making specific claims about electricity sources must disclose the fuel sources of the regional system power mix, net of claims.

4. The State attorney general should be authorized to adopt rules governing any claims regarding the environmental attributes of the retail company itself, of the products it sells or other affirmative marketing claims (including use of the term "green").

5. The State DPU should issue rules to ensure the accuracy and fairness of the disclosure of fuel sources under any mandatory system of disclosure.

III. Quality of Information and Implementation Feasibility

A. Quality of Information

In order for restructured markets to achieve the hoped for environmental benefits, customers will have to know what the differences are between various electricity products and will have to understand the significance of these differences. In other words, consumers will need accurate, meaningful information.

We feel that most of the information that has a significant impact on consumer's decisions will come from marketing claims, not mandatory disclosure labels. Each marketer has the self-interest and the means to explain the relative merits of its product the relatively unfettered freedom to express itself as it chooses. Fortunately, there is a well-established legal framework already in place in all of the states contemplating restructuring and at the federal level to guard against deceptive advertising. Specifically, the Federal Trade Commission (FTC) Act and the state "Little FTC Acts" make unlawful unfair or deceptive practices in or affecting commerce in their various jurisdictions.

Noting the existence of this claims-based "FTC framework" and understanding how it works is important for policymakers and marketers planning competition for electricity. To illustrate the point, recent history in "green marketing" demonstrates that the information disseminated by marketers should be carefully scrutinized because not all marketers are inclined to characterize their products in a meaningful or accurate way. FTC Cases from the past five years tell of toxic antifreeze products being promoted as "eco-safe," and hair sprays containing chlorofluorocarbons as being "ozone friendly." Similarly, experience from the Massachusetts and New Hampshire pilot programs shows how some marketers misleadingly characterized as "hydro" their electricity from pumped storage. Such deceptive advertising in the electricity industry is likely to confuse customers and impair their ability to make rational choices. Confusion may jeopardize the chances of retailers marketing genuinely cleaner electricity to gain market share, and will in turn limit the environmental benefits that can be gained from restructuring.

Therefore, we urge policymakers to make sure the existing federal and state laws are prudently enforced. These efforts can and should be complemented by educational campaigns to raise consumers level of understanding about how electricity is generated and how it impacts our environment and by the efforts of government enforcement agencies (including State attorneys general, public advocates, consumer protection officials and the FTC) and nongovernmental watchdog organizations to guard against false or misleading claims.

In this context, we feel that disclosure regulations may be useful in complementing the existing FTC framework. However, adoption of any disclosure scheme must be conditional upon ensuring that the information in the label: (1) does not unreasonably

distort or limit the accuracy of information disseminated to consumers or limit the meaningfulness of such information, and (2) that marketers' freedom to express the true nature of their electricity is not infringed.

The information in the label should not conflict with other information that marketers are allowed to disseminate about their products. Consider, for example, the system proposed in RAP's model rules for Interim Tracking. Suppose a retailer buys only 10% of its power in a unit contract from a hydro facility, 20% from the power pool, and the remaining 70% from a system contract with Wholesaler A. Suppose also that Wholesaler A's fleet of plants is half gas-powered and half hydro, contributing equally to Wholesaler's available supply. The label under the Interim proposal would show 10 % renewables (hydro) and 90% the pool mix. At the same time, however, and in the same piece of literature, the marketer may be within its rights under FTC rules to claim that at least 80% of its power comes from a mix of natural gas and hydro. As another example, consider a direct mail flyer in which a marketer offers a product that is derived 50% from a new contract with hydropower plant located outside of the region (where there is no similar tracking system to that used in New England) and 50% from a nuclear plant inside the region. The marketer claims in its flyer that its product is 50% renewable and has no SO2, NOx or CO2 emissions. By contrast, the label mandated by RAP's draft interim rule says the product is derived 50% from nuclear generation and 50% from imports and has significant emissions of SO2, NOx and CO2 (i.e., equal to the mix of the exporting region). In both situations, the claim and the label are properly arrived at, but the information conflicts.

Conflicting information is likely to cause consumer confusion and impede the ability of cleaner marketers to differentiate their product from their dirtier competitors. We hope that any disclosure proposals under consideration will avoid as much as possible any potential conflict between what the label requires and what the FTC and the First Amendment allow.

Obviously, the information in the label should also not mislead customers. We do not here take a position on whether a tagging or tracking system is preferable. However, we decline to accept RAP's suggestion that a tag system isless accurate or is somehow more misleading than tracking. It seems to us that RAP's criticism of tags is equally applicable to tracking and to its own proposed hybrid. In a tracking system, it will be nearly as easy for the owner of a nuclear plant to establish a subsidiary that exclusively handles the retail sale of electricity. That subsidiary could offer a variety of products, including a "nuclear free" product, which it would buy various non-nuclear contracts to fulfill, while at the same time selling all of its nuclear generated electricity onto the grid for the spot price. Under RAP's proposed rules the label for the "no-nuke" product would indeed show no nuclear power in its fuel resource mix. This is hardly different, nor any more deceiving or confusing to consumers, than offering a "nuclear-free" product from a company that has sold all of its nuclear generated power onto the grid and purchased tags from a variety of non-nuclear resources. The former is merely more cumbersome and duplicitous. If the criticism is valid for either system, then it seems the proper conclusion is to reject them both as workable options. We think this unnecessary on both counts,

inasmuch as the average consumer will never come face to face with a tag, nor be dissuaded from buying electricity based on a misguided newspaper "expos,," and will in any case be easily reassured if industry members, regulators and watchdog groups help explain the system and how it is verified and audited.

B. Implementation Feasibility

The second condition for any disclosure proposal is that its implemention must be feasible from the perspective of time, administration and cost.

We remain concerned about the administrative feasibility of tracking each transaction necessary to make the hybrid scheme work. While RAP has found one expert who claims the job can readily be handled, other experts from the New England Electric System are adamant that it cannot. Those of us who do not share this area of expertise would feel more comfortable supporting disclosure proposals to the extent we have a better sense of what is truly feasible, particularly given the short time frame with which some states are presented.

Also, we note that as with any proposed regulation, mandatory disclosure presents several legal issues that should be carefully considered. We present in the following section a summary of the issues we identified during the Disclosure meetings and a few observations on the points raised in the RAP final report and draft rules.

IV. Legal Issues

A. Unfair and Deceptive Trade Practices

As we have written previously and noted above, a regulatory framework currently exists that will, if properly enforced, protect consumers against deceptive advertising. The rules against unfair and deceptive trade practices have long been in effect in every state that is considering restructuring. Similar laws are enforced by the Federal Trade Commission and are also available to private litigants by way of the Lanham Act. Moreover, the FTC has promulgated special "Industry Guides" for marketers who plan to make claims about the environmental attributes of their products.

As a general rule, these statutes and Guides make unlawful any false or misleading advertising claim. Among other things, this means that any objective assertion, made expressly or by implication, must not be exaggerated, must not omit any material information, must state the basis of any comparisons, and must be supported by a reasonable basis. This latter requirement, called the "substantiation doctrine," requires that a person making a claim can demonstrate some degree of credible support for the proposition of their claim. For example, an advertiser who says "nine out of 10 doctors recommend our brand" must have some proof, at the time of making the claim, that somebody conducted a reliable poll of doctors and that 9 out of ten in fact recommended this brand.

In section IV of its draft rules, RAP proposes that "LSEs making expressed (sic) or implied marketing claims concerning any aspect of an electricity product included in the label or terms of service ... may substantiate the claims with the information required to be disclosed by this rule." RAP also suggests in the body of the report that the proposed disclosure policy will "protect suppliers from unfair trade practice claims by setting clear rules of the road." In principle, we approve of the concept of coupling disclosure information with the use of either tracking or tags for purposes of substantiating claims about types and quantities of fuels or emissions, and think that the effort to compare past projections with actual performance is a constructive attempt to deal with the difficult issue of obtaining prior substantiation for future performance that cannot be predicted with iron-clad certainty.

However, we wish to point out that the proposed system cannot provide substantiation for all aspects of electricity marketing that may be contained in the label or terms of service and that it will only partially set rules of the road. This is because the proposed label and terms of service will not contain information adequate to support the majority of claims that electricity marketersare likely to make about their products. The proposed disclosure label may well provide substantiation for assertions about the types and quantities of fuels and emissions used to make power, and this is an important contribution to the smooth operation of the system. However, it will not be sufficient to substantiate claims related to the geographical origin of the generation, to many comparative claims, to any special technologies or processes used in the generation (e.g., scrubbers used to reduce emissions), or to the use and impact of off-sets (e.g., planting trees), and it will not provide any rules of the road for suppliers wanting to characterize their product as "green" or "clean," as so many do. These needs will have to be handled some other way.

Also, RAP's recommendation in the body of the report that "factual claims should be explained with enough detail to allow an ordinary customer to understand the basis for the claim" seems to go beyond the requirements of the FTC and equivalent state laws. While it is true that marketers must "possess and rely upon" reasonable evidence to support their claims, the FTC does not mandate explanations to accompany the claim for purposes of substantiation, let alone that there be a standard of detail. What is required, and what RAP has perhaps confused with substantiation, is that explanations accompany claims wherever necessary to avoid a misleading implication of the claim itself. This is different than mandating explanations of how the claim is substantiated. For authority to mandate such a rule, we assume RAP has found something outside of the FTC framework.

B. Compelled Speech

Mandating any type of expression, such as that discussed in the previous section, always implicates free speech rights. As we reported in our earlier research, the Compelled Speech doctrine requires legislators and regulators to proceed with caution when mandating even seemingly incidental representations such as might appear in a label.

The general rule is that regulations of commercial speech will be upheld if they meet the four-step analysis spelled out in the landmark case of Central Hudson. When evaluating compelledspeech regulations, the court must first assure itself that the speech being regulated is in fact commercial speech, and that it does not merit the additional protection afforded to pure speech on the one hand nor the reduced protection given to misleading or unlawful speech on the other. Second, the State must successfully assert a substantial interest to be achieved by restrictions on the speech. The final two steps consider whether the regulatory technique is narrowly tailored to achieve the State interest. Thus, step three is to determine whether the government regulation directly advances the state interest; step four is to determine whether the restriction fashions "a reasonable fit" between the means and the ends. The government has the burden of demonstrating that its regulation survives each prong of the Central Hudson test.

In the executive summary, the body of the report and in particular in the draft rules we note that the stated objectives of the proposed scheme could be bolstered by emphasizing the health, safety and environmental benefits that may be associated with enhanced disclosure. This point is made in the body of the RAP report in the subsection on legal issues, but does not appear to be reflected in the draft rules. We encourage policymakers to reiterate in the objectives or pupose section of any regulations or legislation all relevant state purposes that might be achieved by the proposed disclosure system.

The third and fourth prong of Central Hudson ask whether a mandatory disclosure scheme directly advances the State's purpose(s) and whether the scheme is narrowly tailored. On first impression, it would seem that a carefully crafted disclosure scheme would stand a strong chance of being upheld. First, the Supreme Court has repeatedly noted that more information, not less, is generally helpful in avoiding consumer deception and that the right of a commercial speaker not to divulge accurate information regarding his services is "minimal" and "substantially weaker" than other speech rights. Put differently, the Supreme Court does not think disclosure of "purely factual and uncontroversial information" imposes a heavy inconvenience on commercial speakers. Second, the disclosure scheme need only be "reasonably related" to its ends. Third, the State's scheme need not be the whole solution nor the best solution nor the least restrictive means to achieving its ends.

Still, there are circumstances in which a disclosure scheme could be tripped up if it is not carefully crafted. To prevent this challenge, it may be useful to carefully examine exactly which information should be required in a disclosure label. For example, imports, system and ANI currently serve 37% of the load in New England according to report. If the label scheme does not permit suppliers to reflect attributes of power derived from these sources, but the suppliers are able to find some reasonable way to verify the origins and attributes of that power, then the rulemight benefit from being amended to allow for accurate and meaningful information and thus provide a better "fit" between the means and the ends.

C. Commerce Clause

The Commerce Clause Doctrine is derived from federal law and stands for the proposition that States are limited in their power to erect barriers against interstate commerce. Since much of the electricity transmitted through the power pool crosses state boundaries, it is clear that the Commerce Clause Doctrine is relevant to any analysis of a disclosure scheme.

The Commerce Clause Doctrine addresses two types of regulations. Those that on their face discriminate against interstate commerce must face the highest level of scrutiny. Those that do not facially discriminate against interstate commerce must be tested to determine whether their practical effect is to disadvantage interstate commerce. Facially neutral regulations must meet the following test: (1) that a state or local regulation which does not discriminate against interstate commerce; (2) that it is designed to further a legitimate state interest; and (3) that the burden imposed on interstate commerce is not excessive in relation to the putative local benefits.

The most difficult component of the proposed disclosure scheme from a Commerce Clause perspective seems to be the provision that would treat imports differently from other sources of generation. We feel that in the working groups and in the final report very strong explanations were given for why, generally, imports must be treated differently in order to uphold the integrity of the data and to prevent possible double selling of energy. We also feel that courts may weigh such explanations and deem the proposed systems as the least offensive alternative for achieving the legitimate local interest, but recognize that this is not guaranteed. Indeed, the challenge may be more pronounced if a court were to determine that alternatives such as the FTC framework and state and nongovernmental efforts would provide adequate means to achieve the ends. In this case the court might decide that a disclosure mechanism was not the least offensive alternative to achieve the State interests.

This leaves two other aspects of disclosure to consider under Commerce Clause analysis. First, the provision which allows LSE's to specify the attributes of imported power where there are pre-existing contracts, but to disallow such specification where the contracts are new, seems unjustifiably discriminatory. We find in the report limited explanation as to why this unequal treatment is justified. Second, as noted above, we remain unclear about the magnitude of the burden the hybrid or the full tracking proposals might impose on interstate commerce. Experts of one view suggest the additional administrative and financial burdens are negligible; experts from another say the burdens are nearly insurmountable, at least from the administrative standpoint.

D. Confidentiality

A final issue that merits brief mention is that of confidential business information. In several places the RAP report and draft rules recommend making use of data that is currently submitted to state and federal government agencies, and some circumstances making that information public. While there may be good policy reasons for

implementing these ideas, we are cognizant of the objections of several participants at the Disclosure meetings that some of this information is confidential and may prohibited from being publicized. The rules on confidentiality can be found in the Freedom of Information Act, the Trade Secrets Act, Section 10(a) of the Administrative Procedure Act and in the Federal Rules of Civil Procedures Act. In short, these statutes offer special protections for commercial and financial information that might cause substantial harm to the competitive position of the business should the information be revealed. They specifically prohibit government employees from divulging sensitive business information received by them in the course of their duties (e.g., collecting fuel source and emissions data).

An example relevant to the disclosure proposals comes from the federal circuit courts in Continental Oil Co. v. P.F.C, 519 F.2d 31 (1975). There, a natural gas company objected to disclosure of its prices, names of purchasers, terms and times of price negotiation for every contract. The court found that these intimate details could "alter industry custom and existing relationships to the disadvantage of (the company's) competitive position" and were thus confidential and should not be disclosed. While the federal and state governments clearly have the authority to collect these pieces of data, it is an open question as to whether any of the information mandated to appear in the disclosure labels would be susceptible to the charge that the labels divulge otherwise confidential information.