

ELECTRIC AND GAS UTILITY ADVERTISING: THE FIRST AMENDMENT LEGACY OF *CENTRAL HUDSON*

Contrary to past practice,¹ state public service commissions² now restrict advertising³ by electric and gas public utilities.⁴ Motivated pri-

1. Advertising by energy-producing public utilities was originally encouraged on the belief that due to the efficiency of economies of scale characteristic of public utilities, costs would decrease as sales increased. *See, e.g.*, *West Ohio Gas Co. v. Ohio Pub. Utils. Comm'n*, 294 U.S. 63 (1935); *Dyer v. Missouri Pub. Serv. Comm'n*, 341 S.W.2d 795 (Mo. 1960); *Union Elec. Co.*, 29 PUB. UTIL. REP. (PUR) 3d 254 (Mo. P.S.C. 1959); *Promotional Activities By Gas & Elec. Corps.*, 68 PUB. UTIL. REP. (PUR) 3d 162 (N.Y.P.S.C. 1967).

For a more complete discussion of the economic theory of public utilities, see notes 20-30 *infra* and accompanying text.

2. "Public service commission" may be defined as a legislatively or constitutionally created body charged with the responsibility of regulating costs and profits of public utilities in securing the benefits while avoiding the abuses of natural monopolies. *See* A. FINDER, *THE STATES AND ELECTRIC UTILITY REGULATION* 16-17 (1977). For a more detailed discussion of public service commissions, see notes 31-52 *infra* and accompanying text.

3. Advertising may be defined as "the commercial use, . . . of any media, including newspaper, printed matter, radio, and television, in order to transmit a message to a substantial number of members of the public or to such utility's . . . customers. Public Utilities Regulatory Policies Act of 1978, 16 U.S.C. § 2625(h)(1) (Supp. III 1979) [hereinafter referred to as PURPA]. For a discussion of the purpose and applicability of PURPA, see notes 86-88 *infra*. For purposes of clarity and evaluation, this Note will divide "advertising" into four categories: informational, institutional, political, and promotional. For a sample of alternate divisions of advertising categories, see *Promotional Practices of Elec. Utils.*, 8 PUB. UTIL. REP. (PUR) 4th 268, 273-74 (Fla. P.S.C. 1975) (promotional rates, promotional practices, information, community affairs, institutional); Note, *Public Utilities: The Allowance of Advertising Expenditures for Rate-Making Purposes—Is This Trip Really Necessary?*, 29 OKLA. L. REV. 202, 203 n.5 (1976) (promotional, institutional, consumer); PUB. UTIL. FORT. Mar. 1, 1973, at 47-48 (consumer, conservation, institutional, promotional).

Due to the similarity of content of information, safety, consumer, and conservation advertising, this Note will combine all four into a broad category under the label "informational." *See Re Consumers Power Co.*, No. U-5979 (Mich. P.S.C. Aug. 8, 1980) (allowable informational advertising includes safety, conservation, consumer rate explanation, and factual programs). *Accord*, *Promotional Practices of Elec. Utils.*, 8 PUB. UTIL. REP. (PUR) 4th 268, 275 (Fla. P.S.C. 1975) (informational the same as consumer). For a more complete discussion of the four categories of advertising analyzed in this Note, see notes 82-88 *infra* and accompanying text.

4. "Public utility" is defined as a company operating in such a way as to be "affected with a public interest." *See* E. CLEMENS, *ECONOMICS AND PUBLIC UTILITIES* 12-37 (1950); F. WELCH, *CASES AND TEXT ON PUBLIC UTILITY REGULATION* 1 (1968). *See generally* I. BARNES, *THE ECONOMICS OF PUBLIC UTILITY REGULATION* (1942); Munkirs, Ayers & Grandys, *Rape of the Rate-Payer: Monopoly Overcharges in the 'Regulated' Electric-Utility Industry*, 8 ANTITRUST L. & ECON. REV. 57, 57-58 (1976). The term "public utility" is somewhat of a misnomer in that it "refers only to the nature of the business, not to its ownership or operation . . ." F. WELCH, *supra*. Professor Welch divided public utilities into three main classes of businesses: public trans-

marily by conservationist,⁵ environmental,⁶ and economic⁷ concerns,

portation services for hire, communication for hire, and entities that provide service within the home or place of business. See F. WELCH, *supra*, at 2. He further defined the latter category to include natural gas, manufactured gas, and electric light and power utilities. *Id.* Courts have recognized the following factors as indicia of whether a business entity is a public utility:

- (1) Whether the business devotes property to a public use.
- (2) Whether the business has been regulated in the past.
- (3) Whether a franchise is necessary to enter the business.
- (4) Whether the service rendered is a necessity to the users.
- (5) Whether the business has the characteristics which create monopoly . . .
- (6) Whether excessive competition will exist without public control.

A. LEESTON, J. CRICHTON & J. JACOBS, *THE DYNAMIC NATURAL GAS INDUSTRY* 260-61 (1963) [hereinafter cited as J. JACOBS].

This Note will focus only on the gas and electric energy producing "public utilities." Due to the differences in advertising policies and the distinctive operating nature of gas and electric utilities, telephone, water, and trucking public utilities will not be considered. *Accord*, PUB. UTIL. FORT., Nov. 8, 1979, at 51, 53-54; Note, *supra* note 3, at 203 n.4. It is interesting to note, however, that telephone utility advertising is experiencing similar restrictive policies. See, e.g., *Re Rule Making Relating to Advertising Expenditures*, 39 PUB. UTIL. REP. (PUR) 4th 296 (N.C. Utils. Comm'n 1980). Because this Note will deal only with gas and electric utilities, "utility" means both gas and electric public utilities unless specified otherwise. For further discussion on public utilities, see notes 19-36 *infra* and accompanying text.

Natural gas is a primary fuel source that can be utilized directly for energy consumption. See SUBCOMM. ON ENERGY AND POWER OF THE SENATE COMM. ON INTERSTATE COMMERCE, 96TH CONG., 2D SESS., *THE ENERGY FACTBOOK* 462 (Comm. Print 1980) [hereinafter cited as *THE ENERGY FACTBOOK*]. Electricity, by contrast, is a secondary energy source generated from primary sources such as coal, petroleum (including fuel, oil, crude oil, kerosene and petrol coke), and natural gas and from nuclear and hydro-power sources. See *THE ENERGY SOURCE BOOK* 110 (1977); U.S. DEP'T OF ENERGY, *ELECTRIC POWER SUPPLY AND DEMAND FOR THE CONTIGUOUS UNITED STATES, 1980-1989*, at I.4 (1980) [hereinafter cited as *ELECTRIC POWER SUPPLY*]. See generally U.S. DEP'T OF ENERGY, *ENERGY INFORMATION QUARTERLY REPORT* (1981) [hereinafter cited as *QUARTERLY REPORT*]. Both electric and gas utilities operate under the theoretical construct of economies of scale. See generally R. PIERCE, G. ALLISON & P. MARTIN, *ECONOMIC REGULATION* 448 (1980). In recent years, however, the economies of new plants shifted away from electric utilities because of inflationary effects on fuel and construction costs. See *THE ENERGY SOURCE BOOK*, *supra*, at 92; R. PIERCE, G. ALLISON, & P. MARTIN, *supra*, at 739; notes 104-06 *infra* and accompanying text. The economies of scale for gas utilities remain largely intact.

5. See *Alabama Power Co.*, 97 PUB. UTIL. REP. (PUR) 3d 371 (Ala. P.S.C. 1972); *Southern Cal. Edison Co.*, 100 PUB. UTIL. REP. (PUR) 3d 257 (Cal. P.U.C. 1973); *Public Serv. Co.*, 13 PUB. UTIL. REP. (PUR) 4th 40 (Colo. P.U.C. 1975); *Promotional Practices of Elec. Utils.*, 8 PUB. UTIL. REP. (PUR) 4th 268 (Fla. P.S.C. 1975); *In re Hawaiian Elec. Co.*, 56 Hawaii 260, 535 P.2d 1102 (1975); *Michigan Power Co.*, 18 PUB. UTIL. REP. (PUR) 4th 418 (Mich. P.S.C. 1977); *Southern Union Gas Co.*, 12 PUB. UTIL. REP. (PUR) 4th 219 (N.M.P.S.C. 1975); *Rochester Gas & Elec. Corp.*, 14 PUB. UTIL. REP. (PUR) 4th 475 (N.Y.P.S.C. 1976); *Portland Gen. Elec. Co.*, 8 PUB. UTIL. REP. (PUR) 4th 393 (Or. Pub. Util. Comm'r 1973); *Wisconsin Fuel & Light Co.*, 4 PUB. UTIL. REP. (PUR) 4th 368 (Wis. P.S.C. 1973). See also cases cited in note 107 *infra*.

Concern over conservation was precipitated largely by the 1973 Arab oil embargo. See, e.g., *Notice of Proposal to Issue Order Restricting Certain Uses of Electric Energy*, 13 N.Y. PSC 2074-76 (Dec. 5, 1973) [hereinafter cited as *Notice of Proposal*]. The New York Public Service Commission, assessing what appeared to be a grim energy forecast, stated that "the demands for electric energy in this state cannot be met for the foreseeable future . . ." *Id.* at 2072. *Accord*,

state commissions are implementing these restrictions either by direct prohibition⁸ or by refusal to allocate advertising costs to operating expenses.⁹ Although utilities have responded to these restrictions with various defenses,¹⁰ one defense in particular has fostered constitutional

Duffy, *Public Relations and Advertising Expenses*, PUB. UTIL. FORT., Mar. 31, 1977, at 6, 8 (“[u]ntil the energy crises, most regulatory commissions had no difficulty in recognizing the propriety of any reasonable advertising program as a proper business expense for a public utility”); Netschert, *Then and Now with Utility Advertising and Marketing*, PUB. UTIL. FORT., Nov. 9, 1978, at 17, 17 (“[b]efore the oil embargo, utility advertising was directed at one main objective—load growth”).

Only marginally responsive to conservation efforts, consumption of produced energy continues at increased levels. For example, total electricity annual per capita consumption increased between 1960 and 1976 from 4100 kilowatt hours to 9200 kilowatt hours. FED. ENERGY ADMINISTRATION, *ENERGY IN FOCUS: BASIC DATA*, at VII-1 (1977). Total electricity sales to residential, commercial, and industrial customers increased between 1960 and 1980 from 689 billion kilowatt-hours to 2,094 billion kilowatt-hours. ENERGY INFORMATION ADMINISTRATION, U.S. DEPT OF ENERGY, *ANNUAL REPORT TO CONGRESS, 1980 VOLUME TWO: DATA 161* (1980). Similar patterns exist for consumption of natural gas. Total consumption by residential, commercial, industrial, transportation, and electrical utilities grew between 1960 and 1979 from 11.97 trillion to 20.02 trillion cubic feet of gas. *Id.* at 107.

6. See *Pacific Gas & Elec. Co.*, 87 PUB. UTIL. REP. (PUR) 3d 270 (Cal. P.U.C. 1971); *Public Serv. Co.*, 13 PUB. UTIL. REP. (PUR) 4th 40 (Colo. P.U.C. 1975); *Promotional Practices of Elec. Utils.*, 8 PUB. UTIL. REP. (PUR) 4th 268 (Fla. P.U.C. 1975); *In re Hawaiian Elec. Co.*, 56 Hawaii 260, 535 P.2d 1102 (1975). *Accord*, Duffy, *supra* note 5, at 8 (current concern over advertising due to environmental considerations). See generally Juskow, *Inflation and Environmental Concern: Structural Change in the Process of Public Utility Price Regulation*, 17 J.L. & ECON. 291 (1974); cases cited note 108 *infra*.

7. Economic concerns include growth needs, inflation, and benefits to consumer. See *Promotional Practices of Elec. Utils.*, 8 PUB. UTIL. REP. (PUR) 4th 268 (Fla. P.S.C. 1975); *Michigan Consol. Gas Co.*, 1 PUB. UTIL. REP. (PUR) 4th 229 (Mich. P.S.C. 1973); *Detroit Edison Co.*, 3 PUB. UTIL. REP. (PUR) 4th 209 (Mich. P.S.C. 1974); *Portland Gen. Elec. Co.*, 8 PUB. UTIL. REP. (PUR) 4th 393 (Or. P.U.C. 1974). *Accord*, Duffy, *supra* note 5, at 8 (current concern over advertising due in part to inflation considerations). See generally Juskow, *supra* note 6; cases cited note 109 *infra*.

8. See, e.g., Notice of Proposal, *supra* note 5, at 2074-76. For a partial reproduction of the New York direct prohibition, see note 145 *infra*.

9. For purposes of this Note, cost allocation consists of the process by which a utility expense is passed on to the consumer in the form of rate charges. For a complete discussion of the cost allocation issue, see notes 65-81 & 196-276 *infra* and accompanying text.

10. Utilities traditionally defend advertising expenditures under one of two theories: fourteenth amendment due process claim for undue confiscation of property or assault on management prerogative. The cases supporting the due process defense include *Schneider v. State*, 308 U.S. 147 (1939); *St. Joseph Stock Yards Co. v. United States*, 298 U.S. 38 (1936); *Bluefield Water Works & Improvement Co. v. West Virginia Pub. Serv. Comm'n*, 262 U.S. 679 (1923). Those cases supporting the management prerogative defense include *Alabama Power Co. v. Alabama Pub. Serv. Comm'n*, 359 So.2d 776 (Ala. 1978); *State v. Oklahoma Gas & Elec. Co.*, 536 P.2d 887 (Okla. 1975). See Note, *Advertising by Public Utilities as an Allowable Expense for Ratemaking: Assault on Management Prerogative*, 13 VAL. U.L. REV. 87 (1978). See generally P. GARFIELD & W. LOVEJOY, *PUBLIC UTILITY ECONOMICS* (1964).

debate. By asserting that restrictions on advertising¹¹ operate as a denial of first amendment¹² free speech rights, utilities bring into conflict substantial national concerns: the notion of constitutionally protected free speech versus the nationwide concern over energy conservation, environmental control, and inflation.¹³

The resolution of this conflict is tied directly to the recent United States Supreme Court commercial speech decision in *Central Hudson Gas & Electric Co. v. Public Service Commission*.¹⁴ Commercial speech,¹⁵ which includes utility advertising,¹⁶ is not accorded full first amendment protection.¹⁷ In reaffirming that some first amendment protection exists for commercial speech, the Court in *Central Hudson* established a four-part test.¹⁸ This test is the current standard by which courts must analyze public service commission advertising restrictions.

This Note assesses the impact of the *Central Hudson* test on electric and gas utility advertising and explores the tension between free speech

11. Utilities argue that by a direct prohibition on advertising they are prevented from engaging in that speech. See *Central Hudson Gas & Elec. Co. v. Public Serv. Comm'n*, 447 U.S. 557, 560 (1980). When advertising costs are not allowed in ratemaking, utilities argue that in order to speak they must purchase advertising with constitutionally protected shareholder profits. See *Laclede Gas Co. v. Public Serv. Comm'n*, 600 S.W.2d 222, 226 (Mo. Ct. App. 1980), *appeal dismissed*, 449 U.S. 1072 (1981); *Rochester Gas & Elec. Corp. v. Public Serv. Comm'n*, 64 A.D.2d 345, 410 N.Y.S.2d 142 (1978), *aff'd*, 51 N.Y.2d 823, 413 N.E.2d 359, 433 N.Y.S.2d 420 (1980), *appeal dismissed*, 450 U.S. 961 (1981).

12. The first amendment provides in pertinent part: "Congress shall make no law . . . abridging the freedom of speech . . ." U.S. CONST. amend. I. The first amendment is applicable to the states through the due process clause of the fourteenth amendment. See, e.g., *Bigelow v. Virginia*, 421 U.S. 809, 811 (1975).

13. See notes 107-09 & 208-10 *infra* and accompanying text. Another issue raised by this current regulatory trend is whether the "reasonableness" standard for advertising expenses and deference to management prerogative established in *West Ohio Gas Co. v. Ohio Pub. Util. Comm'n*, 294 U.S. 63 (1935), is still valid. See notes 91-109 & 273-76 *infra* and accompanying text.

14. 447 U.S. 557 (1980).

15. Commercial speech is defined as "speech that does no more than propose a commercial transaction." *Virginia State Bd. of Pharmacy v. Virginia Citizens Consumer Council*, 425 U.S. 748, 771 n.24 (1976); *Pittsburgh Press Co. v. Pittsburgh Comm'n on Human Relations*, 413 U.S. 376, 385 (1973). The Court in *Central Hudson* defined commercial speech slightly differently by stating that it was "expression related solely to the economic interests of the speaker and its audience." *Central Hudson Gas & Elec. Co. v. Public Serv. Comm'n*, 447 U.S. 557, 561 (1980). For a discussion of the commercial speech doctrine, see notes 110-55 *infra* and accompanying text.

16. See *Central Hudson*, 447 U.S. 557 (1980); *Laclede Gas Co. v. Public Serv. Comm'n*, 600 S.W.2d 222 (Mo. Ct. App. 1980), *appeal dismissed*, 449 U.S. 1072 (1981).

17. For a discussion of the first amendment status of commercial speech, see notes 124-51 *infra* and accompanying text.

18. See note 147 *infra*.

rights and energy, environmental, and economic considerations. Part I examines the economic theory of public utility regulation and ratemaking. Part II traces the doctrinal underpinnings of the commercial speech defense from its inception to its apparent culmination in the *Central Hudson* test. Part III then analyzes the degree to which a commercial speech defense protects utility advertising. Finally, Part IV analyzes the question left unresolved by *Central Hudson*: whether reasonableness of the amount of expenditures remains a valid means by which to evaluate utility advertising.

I. REGULATORY ECONOMICS

A. *Natural Monopolies*

The rationale for regulating public utilities is based on the economic concept of natural monopoly. A natural monopoly exists when a "relevant market"¹⁹ has an "indispensable economic need"²⁰ for a product and one firm, rather than two or more, can satisfy that need at the lowest possible cost.²¹ Public utilities are the most common examples of natural monopolies.²²

Economic theory indicates that public utilities will operate most efficiently and produce lower unit costs under a monopoly format.²³ Construction of generating and transmission facilities requires large capital expenditures.²⁴ A protected monopoly is able to make the most efficient use of these capital expenditures for two reasons: monopoly protection "eliminates costly duplication" of generating and transmission

19. Posner, *Natural Monopoly and Its Regulation*, 21 STAN. L. REV. 548 (1969).

20. Munkirs, Ayers & Grandys, *supra* note 4, at 57.

21. Posner, *supra* note 19, at 548. See 2 A. KAHN, THE ECONOMICS OF REGULATION: PRINCIPLES AND INSTITUTIONS 119 (1970). Kahn defines "natural monopoly" as one in which there "is an inherent tendency to decreasing unit costs over the entire extent of the market. This is so only when the economies achievable by a larger output are internal to the individual firm. . . ." *Id.* See generally A. ALCHIAN & W. ALLEN, EXCHANGE AND PRODUCTION, THEORY IN USE 427 (1969).

22. See Posner, *supra* note 19, at 548 ("[t]his set of controls has been applied mainly to gas, water, and electric power companies").

23. See Gabel, Swartz & Zeitlin, *Utility Rates, Consumers, and the New York State Public Service Commission*, 39 ALB. L. REV. 707, 709 (1975) [hereinafter cited as Gabel].

24. See A. FINDER, *supra* note 2, at 3; P. GARFIELD & W. LOVEJOY, *supra* note 10, at 17; Gabel, *supra* note 23, at 709; Meeks, *Concentration in the Electric Power Industry: The Impact of Antitrust Policy*, 72 COLUM. L. REV. 64, 82 (1972). These initial capital expenditures required to construct generating and transmission facilities may also be referred to as fixed costs. Fixed costs are defined as those costs that remain constant regardless of output. Fixed costs may also be referred to as "overhead charges." P. SAMUELSON, ECONOMICS 464-65 (1973).

facilities,²⁵ and, more importantly, when these fixed costs are averaged on a per unit of production basis, average unit costs decrease as output increases.²⁶ Hence, public utilities are subject to the principle of "economies of scale," which means that the cost of each unit becomes cheaper as the utility produces more units.²⁷ Consumers' costs for a utility's services potentially are the lowest when only one firm produces that service within the relevant market. Left unchecked in this competitive void, however, a profit-maximizing²⁸ public utility is free to exploit its market position by charging exorbitant prices.²⁹ To curb this otherwise uncontrolled power and its potential for pricing abuse, state legislatures created public service commissions.³⁰

25. Gabel, *supra* note 23, at 709.

26. See A. FINDER, *supra* note 2, at 3; P. GARFIELD & W. LOVEJOY, *supra* note 10, at 18; 1 A. KAHN, *supra* note 21, at 45-46.

27. See 1 A. KAHN, *supra* note 21, at 11. Due to economic and social changes, the principle of economies of scale is of less significance today, especially as to electric utilities. See notes 99-100 *infra* and accompanying text.

28. See Munkirs, *supra* note 4, at 58.

29. See A. ALCHIAN & W. ALLEN, *supra* note 21, at 427; 1 A. KAHN, *supra* note 26, at 27-28.

30. See A. FINDER, *supra* note 2, at 16-17. In theory, the development of the public service commissions was designed to stimulate the forces of competition that occur in a competitive market. 1 A. KAHN, *supra* note 26, at 17; 1 A. PRIEST, *PRINCIPLES OF PUBLIC UTILITY REGULATION* 1-2 (1969). Thus, the regulatory commission acts as a surrogate competitor. *Cantor v. Detroit Edison Co.*, 428 U.S. 579, 595-96 (1976).

The historical development of public service commissions began with the common-law state police power under which was created the "power of the state to do things to protect and promote the health and welfare of its citizens." F. WELCH, *supra* note 4, at 3. This limited basis for regulation gained additional support in the Supreme Court's landmark decision in *Munn v. Illinois*, 94 U.S. 113 (1877). See A. FINDER, *supra* note 2, at 16; F. WELCH, *supra* note 4, at 1. In *Munn* the Supreme Court upheld the authority of the Illinois legislature to regulate rate ceiling for those businesses "affected with a public interest." 94 U.S. at 126.

Nevertheless, the state legislative authority to regulate businesses "affected with the public interest" was circumscribed to purely intrastate transactions in a subsequent opinion. See *Wabash, St. L. & P. Ry. v. Illinois*, 118 U.S. 557 (1886). This decision confirmed the authority of the federal government to regulate interstate commerce. As a result of *Wabash*, state legislatures were powerless to regulate organizations engaging in interstate commerce. This void was filled by the creation of the Interstate Commerce Commission (ICC) in 1877. Creation of the ICC was important for two reasons: it made possible the regulation of public utilities not solely engaged in intrastate activity, and the structure and organization of the ICC served as a model for the impending state regulatory commissions. See A. FINDER, *supra* note 2, at 16.

In response to these developments, the Georgia, New York, and Wisconsin legislatures in 1907 established the first state public service commissions. *Id.* Even though their regulation was limited to intrastate activity, the subsequent creation of the Federal Power Commission and its corresponding regulations "limited the development of electric and gas utilities to statewide systems," effectively giving control of public utilities to the states. *Id.* at 17.

B. *Public Service Commissions*

Public service commissions³¹ of one form or another exist in all fifty states and the District of Columbia.³² Creation of these regulatory bodies is either by state legislative³³ or constitutional³⁴ authority. Commission size varies from one commissioner³⁵ to seven,³⁶ with most states having between three to five commission members.³⁷ Members' terms of office, which are often staggered,³⁸ range from four³⁹ to eight years,⁴⁰ with selection varying from gubernatorial appointment⁴¹ to statewide election.⁴² To neutralize the politics of the decision making process of public service commissions, some states regulate the political composition of the membership.⁴³ In all but nine states, service on the

31. The term "public service commission" for purposes of this Note will be used synonymously with "regulatory commission" and "commission."

32. For purposes of clarity and continuity, the Virgin Islands and Puerto Rico, though territories of the United States, are omitted from consideration in this Note. Puerto Rico, however, does have a three-member public service commission with members serving four-year terms. Selection is by gubernatorial appointment with senatorial approval. Members serve on a full-time basis. See A. FINDER, *supra* note 2, at 18.

The Virgin Islands has a nine-member commission appointed by the governor to serve three-year staggered terms. See *id.*

33. See, e.g., ALA. CODE § 37-1-1 (1975); FLA. STAT. ANN. § 350.01 (West 1968); HAWAII REV. STAT. § 269-2 (1976); ILL. REV. STAT. ch. 111-2/3, § 1 (1973); MASS. ANN. LAWS ch. 25, § 1 (Michie/Law. Co-op 1980); MO. REV. STAT. § 386.040 (1978); N.J. STAT. ANN. § 48:2-1 (West Supp. 1974); OHIO REV. CODE ANN. § 4901.02 (Page Supp. 1980); UTAH CODE ANN. § 54-1-1 (1974).

34. See, e.g., CAL. CONST. art. XII, § 22; GA. CONST. § 2-2703; VA. CONST. art. IX, § 1.

35. See OR. REV. STAT. § 756.020 (1974) (single commissioner).

36. See S.C. CODE § 58-3-10 (1976) (seven commissioners).

37. Those commissions having three members include: VA. CONST. art. IX, § 1; ALA. CODE § 1 (1975); FLA. STAT. ANN. § 350.01 (West 1968); OHIO REV. CODE ANN. § 4901.02 (Page Supp. 1980); UTAH CODE ANN. § 54-1-1 (1974).

38. See, e.g., CAL. CONST. art. XII, § 22; ALA. CODE § 37-1-3 (1975); UTAH CODE ANN. § 54-1-1.5 (1974); VA. CODE § 12.1-6 (1973).

39. See, e.g., ALA. CODE § 37-1-3 (1975); FLA. STAT. ANN. § 350.01 (West 1968); HAWAII REV. STAT. § 26-34 (1976); OR. REV. STAT. § 756.020 (1974).

40. See N.C. GEN. STAT. § 62-10(b),(c) (Cum. Supp. 1981). Other states fall somewhere between the two extremes. CAL. CONST. art. XII, § 22 (six years); ILL. REV. STAT. ch. 111-2/3, § 1 (1973) (five years); MASS. ANN. LAWS ch. 25, § 2 (Michie/Law. Co-op 1980) (coterminous with governor); OR. REV. STAT. § 756.020 (1974). Of the above states, all but Oregon require senate advice or approval of the governor's selection. See A. FINDER, *supra* note 2, at 18.

41. See A. FINDER, *supra* note 2, at 18.

42. See, e.g., GA. CONST. § 2-2703; N.D. CONST. art. V, § 12; ALA. CODE § 37-1-3 (1975); FLA. STAT. ANN. § 350.01 (West 1968).

43. See, e.g., ILL. REV. STAT. ch. 111-2/3, § 1 (1973); MASS. ANN. LAWS ch. 25, § 2 (Michie/Law. Co-op 1980); OHIO REV. CODE § 4901.02 (Page Supp. 1980).

commission is a full-time position.⁴⁴ The fundamental task of the public service commissions is to secure the benefits of a natural monopoly while preventing the inherent abuses.⁴⁵

Public service commissions regulate utility advertising primarily through ratemaking.⁴⁶ Ratemaking is the process in which regulatory commissions strive to simulate the effects of a competitive market by controlling profits.⁴⁷ Waste is an inevitable consequence of artificial profit control.⁴⁸ Because utilities are guaranteed a profit,⁴⁹ they have little incentive to minimize costs.⁵⁰ This likelihood of wasteful spending compels regulatory commissions to control utility expenses as well as profits. Because utilities include some advertising expenses in their cost accounts,⁵¹ commissions must accordingly eliminate wasteful ad-

44. See A. FINDER, *supra* note 2, at 18. The nine states not having full-time commission members are Delaware, Hawaii, Kentucky, Louisiana, Maryland, Massachusetts, New Jersey, Rhode Island, and Vermont. *Id.* Massachusetts, Rhode Island and Vermont, however, do have full-time commission chairpersons. *Id.*

45. See A. FINDER, *supra* note 2, at 17.

46. For a complete discussion of the theory and process of ratemaking, see J. BONBRIGHT, *PRINCIPLES OF PUBLIC UTILITY RATES* 147-283 (1966); I. A. KAHN, *supra* note 26, at 20-57; I. A. PRIEST, *supra* note 30, at 45-226. See also notes 56-115 *infra* and accompanying text.

Regulation of utility advertising may be achieved by public service commission policy statements. See notes 163-95 *infra* and accompanying text.

Ratemaking is distinguishable from rate regulation despite their similarities. Rate regulation is a broad term that may include the specific act of ratemaking. Generally, rate regulation and ratemaking differ in timing. Ratemaking is initiated when a utility files for a rate increase. See, e.g., CAL. PUB. UTIL. CODE §§ 486, 495 (Deering 1970); HAWAII REV. STAT. § 269-16 (1976); MASS. ANN. LAWS ch. 159, § 19 (Michie/Law. Co-op 1979); UTAH CODE ANN. § 54-3-2(2) (1973). Once this rate schedule is on file, it is subject to challenge either by regulatory commissions or by independent sources. See, e.g., CAL. PUB. UTIL. CODE § 455 (Deering 1970); OHIO REV. CODE ANN. § 4909.27 (Page Supp. 1977); OR. REV. STAT. §§ 756.500, .515 (1979). Once challenged, the rates are subject to alteration by the commission should the charges be deemed unreasonable. See, e.g., FLA. STAT. ANN. §§ 364.14, 366.07 (West 1968); MASS. ANN. LAWS ch. 164, § 94 (Michie/Law. Co-op Supp. 1974); UTAH CODE ANN. § 54-4-2 (1974).

47. See I. A. KAHN, *supra* note 26, at 17.

48. See Posner, *supra* note 19, at 601-02. According to Posner, "[r]egulation may encourage other wasteful expenditures. Management can react in two ways to a ceiling on profits. It can charge the price that will return the allowed profit and not more. Or it can charge the monopoly price but convert the forbidden profit into increased cost." *Id.*

49. Under the rule in *Smyth v. Ames*, 169 U.S. 466 (1898), a utility is granted a "fair return upon the value of that which it employs for the public convenience." *Id.* at 547. See notes 54-63 *infra* and accompanying text.

50. See A. ALCHIAN & W. ALLEN, *supra* note 21, at 428.

51. See A. FINDER, *supra* note 2, at 46-47; W. JONES, *CASES AND TEXT ON REGULATED INDUSTRIES* 183-84 (1967); I. A. PRIEST, *supra* note 30, at 45-46, 191-93; Jones, *An Example of a Regulatory Alternative to Antitrust: New York Utilities in the Early Seventies*, 73 COLUM. L. REV. 462, 480 (1973).

vertising expenditures.⁵²

C. *Ratemaking*

1. *Constitutional Underpinnings*

*Smyth v. Ames*⁵³ governs the process of establishing rates. *Smyth* guarantees the utility a "fair return on the fair value" of its product.⁵⁴ The *Smyth* Court, however, left open the precise meaning of "fair value" and "fair return."⁵⁵ After years of shifting doctrine,⁵⁶ the Supreme Court settled these ambiguities in *Bluefield Water Works & Improvement Co. v. West Virginia Public Service Commission*⁵⁷ and *Federal Power Commission v. Hope Natural Gas Co.*⁵⁸ Emphasizing the "end result"⁵⁹ of rate setting, the *Hope* Court declared that the legal standard for "fair value" is the dollar value of the depreciated original

52. See Jones, *supra* note 51, at 477. Professor Jones, in discussing wasteful expenditures, noted that "such high rates and profits generally should be disallowed to prevent monopolistic exploitation of consumers . . ." *Id.*

53. 169 U.S. 466 (1898).

54. *Id.* at 547. The Court noted that in order for a utility "to earn a fair return on the value" of its investment, reasonable rates must be set. *Id.* The opinion in *Smyth* was a precursor of the subsequent comparable earnings test stated in *Bluefield Water Works Co. v. West Virginia Pub. Serv. Comm'n*, 262 U.S. 679 (1923), and *Federal Power Comm'n v. Hope Natural Gas Co.*, 320 U.S. 591 (1944). See generally 1 A. PRIEST, *supra* note 30, at 191-94; Jones, *supra* note 51.

55. The Court refused to choose between one of three methods of evaluation of the "fair value" standard: original cost, market value of stocks and bonds, and present cost of construction. See J. JACOBS, *supra* note 4, at 268.

56. See *id.* In the 46-year interim between *Smyth* and *Hope*, the Court went from a focus on reproduction costs to the creation of the "prudent investment" theory in a dissenting opinion in *Southwestern Bell Tel. Co. v. Public Serv. Comm'n*, 262 U.S. 276, 306-07 (1923) (Brandeis and Holmes, JJ., dissenting). In 1933 the Court reaffirmed the reproduction costs approach in *Los Angeles Gas & Elec. Co. v. California R.R. Comm'n*, 289 U.S. 287, 307-08 (1933).

57. 262 U.S. 679 (1923). The Supreme Court, in giving meaning to "rate of return," established a specific standard expressing a policy ensuring a utility's guaranteed profit and an ability to attract capital:

A public utility is entitled to such rates as will permit it to earn a return on the value of the property which it employs for the convenience of the public equal to that generally being made at the same time and in the same general part of the country on investments in other business undertakings which are attended by corresponding risks and uncertainties; but it has no constitutional right to profits such as are realized or anticipated in highly profitable enterprises or speculative ventures. The return should be reasonably sufficient to assure confidence in the financial soundness of the utility and should be adequate, under efficient and economical management, to maintain and support its credit and enable it to raise the money necessary for the proper discharge of its public duties. . . ."

Id. at 692-93.

58. 320 U.S. 591 (1944).

59. *Id.* at 603.

investment.⁶⁰ The Court further clarified that the "fair return" aspect of the *Smyth* decision requires a level of return sufficient to pay interest on debt and dividends on preferred stock and to maintain the firm's financial integrity.⁶¹

Accordingly, under the *Smyth-Bluefield-Hope* analyses, the primary objective in ratemaking is to set rates so that the utility will be able to meet its legitimate operating expenses as well as to pay creditors and provide dividends to shareholders.⁶² The utility's return should be sufficient to maintain its financial integrity so that it might attract new capital.⁶³ Most state regulatory commissions use this judicially developed approach.⁶⁴

The most frequent implementation⁶⁵ of the objectives established in the *Smyth-Bluefield-Hope* trilogy occurs when a utility files a new rate schedule.⁶⁶ After the utility files a rate request, the commission evaluates the requested rates, usually at a hearing.⁶⁷ The figures discussed in the ratemaking process are based on "test year" results—actual detailed financial information from a previously recorded year of operation.⁶⁸ The test year figures that have commission approval are then

60. *Id.* at 603-05. See 1 A. PRIEST, *supra* note 30, at 142-56; Jacobs, *supra* note 4, at 268. "Original cost," now a term of art, has been defined as the "cost of an asset when first devoted to public service." J. BONBRIGHT, *supra* note 46, at 174 n.2. Most jurisdictions follow the "original cost" approach, although a decided minority still uses a "fair value" formula based on actual cost. *Id.* at 158-71.

61. 320 U.S. at 603. The *Hope* Court noted: "[I]t is important that there be enough revenue not only for operating expenses but also for the capital costs of the business. . . . That return, moreover, should be sufficient to assure confidence in the financial integrity of the enterprise, so as to maintain its credit and to attract capital . . ." *Id.* See 1 A. PRIEST, *supra* note 30, at 191-92; Jones, *supra* note 51, at 477. The "fair return" aspect of *Smyth* and *Hope* was developed by the Supreme Court in *Bluefield*. See note 57 *supra*.

62. 320 U.S. at 603; 262 U.S. at 692-93; 169 U.S. at 544. See Jones, *Judicial Determination of Public Utility Rates: A Critique*, 54 B.U.L. REV. 873, 875 (1974).

63. 320 U.S. at 603, 605; 262 U.S. at 693. See Jones, *supra* note 51, at 477.

64. See A. FINDER, *supra* note 2, at 25.

65. Most rate issues arise during the actual process of ratemaking. Nevertheless, complaints may be filed about existing rates either upon initiative of an independent source or motion of a regulatory commission. See note 46 *supra*.

66. See, e.g., N.Y. PUB. SERV. LAW § 66(12) (McKinney Supp. 1975-76).

67. See A. FINDER, *supra* note 2, at 23; J. JACOBS, *supra* note 4, at 267; Gabel, *supra* note 23, at 718.

68. See J. BONBRIGHT, *supra* note 46, at 150 n.7; 1 A. PRIEST, *supra* note 30, at 45; Jones, *supra* note 51, at 477. The test year is frequently the 12 months immediately preceding rate determination. See 1 A. PRIEST, *supra* note 30, at 45. However, the year most often selected is the most recent one for which complete data is available. See Gabel, *supra* note 23, at 720 (the year for which total data is determinable); Huntington, *The Rapid Emergence of Marginal Cost Pricing*

injected into the traditional ratemaking formula refined from principles set out in the *Smith-Bluefield-Hope* trilogy: (rate base \times rate-of-return) + operating expenses = revenue.⁶⁹ The revenue component represents the total dollar amount a utility may legally receive from the retail rates it charges consumers.⁷⁰ The rate base is the formula that expresses the *Smyth* "fair value" requirement.⁷¹ In most jurisdictions,⁷² the rate base is the sum of the utility's original investment and the working capital

in the Regulation of Electric Utility Rate Structures, 55 B.U.L. REV. 689, 699 (1975) (selection of test year for which detailed financial information on company's operations is available); Jones, *supra* note 62, at 876 (most recent annual period for which complete financial data is available); Posner, *supra* note 19, at 592 (ordinarily the most recent typical year of operation for which complete data are available).

In *West Ohio Gas Co. v. Public Utils. Comm'n*, 294 U.S. 79 (1935), Justice Cardozo emphatically rejected the notion of basing ratemaking on a single test year: "[A]doption of a single year as an exclusive test or standard imposed upon the company [is] an arbitrary restriction in contravention of the Fourteenth Amendment and of the 'rudiments of fair play' made necessary thereby." *Id.* at 81. Furthermore, the "test year" need not be wholly "historical." See I A. PRIEST, *supra* note 30, at 45; Gabel, *supra* note 23, at 720. Some have called for a future or projected test year. See Note, *The Use of the Future Test Year in Utility Rate-Making*, 52 B.U.L. REV. 791 (1972). The more common solution, however, is to use a test year based partly on historical experience and partly on projected figures. See I A. PRIEST, *supra* note 30, at 45; Gabel, *supra* note 23, at 720; Jones, *supra* note 62, at 880.

Due to inflation and other factors, the test year figures may not accurately represent normal conditions. As a result, adjustments must be made in the data. See Huntington, *supra*, at 699 (citing rate increases, wage increases, tax consequences, and environmental compliance costs as factors requiring adjustments in test year data); Jones, *supra* note 62, at 877 (citing abnormal conditions such as labor disturbances, unusual weather, or atypical equipment outages as factors). See generally I A. PRIEST, *supra* note 30, at 45. For a criticism of test year data use, see Posner, *supra* note 19, at 593-94.

69. Pontz & Sheller, *The Consumer Interest—Is it Being Protected by the Public Utility Commission?*, 45 TEMP. L.Q. 315 (1972). The same components have been expressed in slightly varying formulas by other sources. See also J. JACOBS, *supra* note 4, at 267. Jacobs expressed the formula in the following format: $R = E + (v) r + d + T$, when R = revenue to be received from the rates in question; E = annual operating expense; v = value of the physical property; r = rate of return, expressed as a fraction; d = current annual depreciation; and T = taxes. *Id.* at 267.

70. See J. JACOBS, *supra* note 4, at 267; Pontz & Sheller, *supra* note 69, at 316. The amount of revenue represented by R does not represent a guaranteed amount, but rather the amount a utility has an opportunity to earn. I A. PRIEST, *supra* note 30, at 46, 191.

71. See Gabel, *supra* note 23, at 720.

72. See note 60 *supra* and accompanying text. Professor Bonbright defined "original cost" as the "cost of an asset when first devoted to public service rather than cost to a transferee company." J. BONBRIGHT, *supra* note 46, at 174 n.2. Currently thirty-six state commissions employ the "original cost" method. See A. FINDER, *supra* note 2, at 38. A decided minority of 13 state commissions abides by the "fair value" rate base method. *Id.* at 39. Fair value jurisdictions compute rate base on utility property "used and useful." I A. PRIEST, *supra* note 30, at 46. Hence, fair value jurisdictions consider more than just "original cost" in computing rate base figures. See *Missouri Water Co. v. Public Serv. Comm'n*, 308 S.W.2d 704 (Mo. 1957). *Accord*, *Joplin Water Works Co. v. Public Serv. Comm'n*, 495 S.W.2d 433 (Mo. 1973).

allowance⁷³ less accumulated depreciation.⁷⁴

When determining a utility's rate-of-return, a commission must satisfy the *Hope* and *Bluefield* policy requirements of maintaining and supporting credit and attracting capital investment.⁷⁵ Commissions usually determine rate-of-return by the "cost of capital" approach.⁷⁶ Under this method, a commission inspects the capital structure of a utility to determine cost of debt, preferred stock, and common stock.⁷⁷ By making the appropriate calculations,⁷⁸ the commission may then determine the appropriate rate-of-return.

The final element of the ratemaking formula is operating expenses,⁷⁹ which include such costs as labor, maintenance, materials, supplies,⁸⁰ and advertising.⁸¹

2. Advertising

Public utilities employ four general types⁸² of advertising: informational, institutional, political, and promotional. Informational adver-

73. See F. WELCH, PREPARING FOR THE UTILITY RATE CASE 160-61 (1954). Working capital represents the amount of cash needed to satisfy day-to-day expenses in the normal operations of the utility. See P. GARFIELD & W. LOVEJOY, *supra* note 10, at 71; F. WELCH, *supra*, at 195. For example, if for an appropriate test year the original cost of plant investment were \$50 million and accrued depreciation on that investment were \$5 million and an allowance was granted of \$3 million for working capital, the rate base for the utility would be \$48 million. This amount of rate base is then multiplied by the appropriate rate-of-return percentage. Technically, rate of return is represented as a percentage of the rate base. See 1 A. PRIEST, *supra* note 30, at 46; F. WELCH, *supra* note 73, at 201.

74. For a discussion rate base determination, see J. BONBRIGHT, *supra* note 46, at 172-91; 1 A. KAHN, *supra* note 26, at 35-41.

75. See note 61 *supra* and accompanying text.

76. See J. BONBRIGHT, *supra* note 46, at 240-56; 1 A. PRIEST, *supra* note 30, at 208-10; Jones, *supra* note 62, at 881.

77. See Jones, *supra* note 62, at 881.

78. This computation is best explained by Professor Jones' example: If the utility had a capital structure consisting of 50% debt, 15% preferred stock, and 35% common stock and the commission determined the cost of debt to be 6%, the cost of preferred stock to be 8%, and the cost of common stock 12%, then the composite cost of capital can be calculated.

Debt	50% at 6% =	.030
Preferred Stock	15% at 8% =	.012
Common Stock	35% at 12% =	.042
		<u>.084</u>

The composite cost of capital is .084 or 8.4%. *Id.* at 881.

79. See Gabel, *supra* note 23, at 723.

80. *Id.*

81. See note 51 *supra* and accompanying text. An expense included in the rate formula may also be referred to as "above-the-line."

82. See note 3 *supra*.

tising is designed to inform consumers about everyday services, safety precautions, conservation measures, and rate changes.⁸³ Institutional advertising, also known as goodwill advertising because of its goal of fostering goodwill toward the public utility,⁸⁴ is "designed to enhance or preserve the corporate image of the utility."⁸⁵ Political advertising⁸⁶ includes "advertising for the purpose of influencing public opinion with respect to legislative, administrative, or electoral matters, or with respect to any controversial issue of public importance."⁸⁷ Finally,

83. See PUB. UTIL. FORT., Mar. 1, 1973, at 47; Note, *supra* note 10, at 118. The New York Public Service Commission has included "time-of-day" advertising in its definition of informational advertising: "We recognize, however, that as we move toward more and more widespread adoption of time of day rates, it may be highly desirable for companies to publicize those rates. . . . [T]his advertising may better be described as informational. . . ." Notice of Proposal, *supra* note 5, at 2-R, 3-R. Informational advertising may also be referred to as "consumer," "safety," or "conservation" advertising. See PUB. UTIL. FORT., Mar. 1, 1973, at 47; note 3 *supra*.

The Idaho Public Utilities Commission defines informational advertising as "advertising which encourages safety, promotes conservation, or fosters the proper use of electrical appliances, [and] confers actual benefits upon ratepayers. . . ." *Re Idaho Power Co.*, 29 PUB. UTIL. REP. (PUR) 4th 183, 204 (Idaho P.U.C. 1979). *Accord*, *Arkansas Power & Light Co.*, 15 PUB. UTIL. REP. (PUR) 4th 153 (Ark. P.S.C. 1976); *Re Consumers Power Co.*, No. U-5979 (Mich. P.S.C. Aug. 8, 1980); *Southern Union Gas Co.*, 12 PUB. UTIL. REP. (PUR) 4th 219 (N.M.P.S.C. 1975).

84. See *Re Public Serv. Co.*, No. 2548 (N.H.P.S.C. July 31, 1980) (institutional advertising promotes goodwill of utility); Brief for Appellant at 18, *Laclede Gas Co. v. Public Serv. Comm'n*, 600 S.W.2d 222 (Mo. Ct. App. 1980), *appeal dismissed*, 449 U.S. 1072 (1981) (institutional advertising referred to as "goodwill advertising"); Note, *supra* note 10, at 117.

85. See PUB. UTIL. FORT., Mar. 1, 1973, at 47. *Accord*, *Re Washington Gas Light Co.*, 39 PUB. UTIL. REP. (PUR) 4th 161 (D.C.P.S.C. 1980); *Re Tampa Elec. Co.*, 39 PUB. UTIL. REP. (PUR) 4th 553 (Fla. P.S.C. 1980); *Re Promotional Practices of Pub. Util. & Coop. Util. Ass'ns*, 97 PUB. UTIL. REP. (PUR) 3d 1 (Okla. Corp. Comm'n 1972). Institutional or goodwill advertising focuses on aspects other than selling a product. G. FLANIGAN, MODERN INSTITUTIONAL ADVERTISING 3-4 (1967).

86. One writer classified advertising of a political nature under the broad heading of institutional advertising. Ciscel, *Tempest in a Teapot: Utility Advertising*, PUB. UTIL. FORT., Aug. 12, 1976, at 35, 37. Nevertheless, the recent judicial focus on utility advertising of a political nature and Congress' separate treatment of political advertising in Titles I and III of PURPA seems to warrant the decision to treat political advertising as a separate category. See 15 U.S.C. § 3203(b)(1)(B) (Supp. III 1979); 16 U.S.C. § 2625(h)(1)(B) (Supp. III 1979). *Accord*, *First Nat'l Bank of Boston v. Bellotti*, 435 U.S. 765 (1978); *Re Washington Gas Light Co.*, 39 PUB. UTIL. REP. (PUR) 4th 161 (D.C.P.S.C. 1980); *Re Rule Making Relating to Advertising Expenditures*, 39 PUB. UTIL. REP. (PUR) 4th 295 (N.C. Utils. Comm'n 1980); *Re The Narragansett Elec. Co.*, 23 PUB. UTIL. REP. (PUR) 4th 509 (R.I.P.U.C. 1978). Political advertising may also be referred to as controversial issue advertising. See *Re Rule Making Relating to Advertising Expenditures*, 39 PUB. UTIL. REP. (PUR) 4th 295 (N.C. Utils. Comm'n 1980).

87. 15 U.S.C. § 3203(b)(1)(B) (Supp. III 1979); 16 U.S.C. 2625(h)(1)(B) (Supp. III 1979). Even though PURPA does not expressly preempt state authority to conduct ratemaking, it nevertheless serves as an influential federal factor in state rate proceedings. See Note, *Title I of PURPA: The Effect of Federal Intrusion into Regulation of Public Utilities*, 21 WM. & MARY L.

public utilities engage in promotional advertising, which encourages the use of a utility's services or the use of appliances or equipment designed to use the utility's services.⁸⁸

In order to prevent a utility from exploiting its monopoly position,⁸⁹ the operating expense element of the ratemaking formula can include only those advertising expenses that are reasonable.⁹⁰ The Supreme Court developed the reasonableness standard in *West Ohio Gas Co. v. Ohio Public Utilities Commission*.⁹¹ The Court held that commissions must accord management discretion a presumption of validity⁹² and

REV. 491, 505-06 (1979). Submitted in 1977 as part of President Carter's national energy plan, PURPA embodies a proposal to reform retail electric and gas rate design by providing federally uniform standards for public utilities. See Wagner, *Multiple Referral: House Energy Bill*, 35 CONG. Q. WEEKLY REP. 841 (1977).

PURPA requires state regulatory agencies to assess whether the federal standards would further the Act's purpose if implemented by the state. See 16 U.S.C. § 2621 (Supp. III 1979). If the Act's standards conflict with existing state law, a state is not required to adopt the Act. 16 U.S.C. § 2623 (Supp. III. 1979). See, e.g., *Re Determination of Whether Advertising Rules Conform to Pub. Util. Regulatory Policies Act of 1978*, No. 35723 (Ind. P.S.C. Jan. 16, 1980) (commission noting state policies consistent with Act's purpose); *Re Consolidated Edison Co.*, No. 80-8 (N.Y.P.S.C. Mar. 7, 1980) (declining adoption of PURPA due to conflict in policy on promotional advertising). It is interesting to note that PURPA expressly proscribes promotional and political advertising costs from being passed on in consumer rates. 16 U.S.C. § 2623(h) (Supp. III 1979). At least one court has declared PURPA unconstitutional. See *Mississippi v. Federal Energy Regulatory Comm'n*, 38 PUB. UTIL. REP. (PUR) 4th 284, 287-88 (S.D. Miss. 1981) (*Miss. Power & Light Co.*, intervenor), *prob. juris. noted*, 49 U.S.L.W. 3930 (U.S. argued Jan. 19, 1982) (No. 80-1749). The Mississippi federal district court indignantly declared: "The sovereign state of Mississippi is not a robot, or lackey which may be shuttled back and forth to suit the whim and caprice of the federal government, but was and is the prime benefactor of the power and authority designated by the Constitution . . ." *Id.* at 285.

88. See 15 U.S.C. § 3203(b)(1)(C) (Supp. III 1979); 16 U.S.C. § 2625(h)(1)(C) (Supp. III 1979). The New York Public Service Commission defined promotional advertising as "advertising intended to stimulate the purchase of the utility services." See *Central Hudson Gas & Elec. Co. v. Public Serv. Comm'n*, 447 U.S. 557 (1980). *Accord*, PUB. UTIL. FORT., Mar. 1, 1973, at 47; Note, *supra* note 10, at 106.

The definitions provided in Titles I and III of PURPA are not mandatorily imposed on state commissions. Rather, the definitions provide an authoritative federal view and suggest appropriate guidelines for dealing with gas and electric advertising and rates. See note 86 *supra*.

The PURPA definition of promotional advertising, which includes the promotion of sale and use of energy-using appliances, accords with regulatory commission policy. See *Re Tampa Elec. Co.*, 39 PUB. UTIL. REP. (PUR) 4th 553 (Fla. P.S.C. 1980); *Re Idaho Power Co.*, 29 PUB. UTIL. REP. (PUR) 4th 183 (Idaho P.S.C. 1979); *Re Rule Making Relating to Advertising Expenditures*, 39 PUB. UTIL. REP. (PUR) 4th 295 (N.C. Utils. Comm'n 1980).

89. See notes 51-52 *supra* and accompanying text.

90. For a discussion of the "reasonableness" standard, see notes 91-109 *infra* and accompanying text.

91. 294 U.S. 63 (1935).

92. *Id.* at 72. Justice Cardozo, writing for the majority, stated:

that regulatory commissions can disallow advertising expenses only if those expenses are a by-product of inefficiency or improvidence.⁹³

After *West Ohio Gas*, courts consistently overturned arbitrary regulatory commission decisions that had disallowed advertising cost allocation.⁹⁴ As a result, regulatory commissions readily accepted advertising outlays between 1935 and the early 1970s.⁹⁵ During this period of laissez-faire utility advertising regulation, the principle of economies of scale operated at its zenith of efficiency.⁹⁶ Growth and consumption were desirable elements for utilities.⁹⁷ Hence, advertising that stimulated growth received broad approval.⁹⁸

In the early 1970s regulatory commissions abruptly changed this pol-

The commission did not question the fact of payment, but cut down the allowance . . . on the ground that anything more was unnecessary and wasteful. The criticism has no basis in evidence, either direct or circumstantial. Good faith is to be presumed on the part of the managers of a business.

Id. (citations omitted).

93. *Id.* at 72. Justice Cardozo added: "The presumption of correctness that gives aid in controversies of this order . . . was confined in this instance by what amounts to a finding of regularity. . . . A public utility will not be permitted to include negligent or wasteful losses among its operating charges." *Id.* at 68.

Important burdens of proof were also delineated in *West Ohio Gas*. Because the utility has a monopolistic edge on the public, it traditionally has the initial burden of proof in seeking a rate increase. *El Dorado v. Arkansas Pub. Serv. Comm'n*, 235 Ark. 812, 362 S.W.2d 680 (1962). *West Ohio Gas* established that this burden may be met upon a showing of an expense paid. Furthermore, the Court in *West Ohio Gas* stated that once the utility satisfies its burden, the burden shifts to the commission to prove the cost "unnecessary or wasteful." 294 U.S. at 72. The standard of proof set out in *West Ohio Gas* was adopted in a different form by an Idaho court in *Boise Water Corp. v. Idaho Pub. Utils. Comm'n*, 97 Idaho 832, 837, 553 P.2d 163, 171 (1976) (utility burden of production met by a showing of actual incurrence of expense; burden shifted to commission to show expenses unreasonable).

94. See, e.g., *City of El Dorado v. Arkansas Pub. Serv. Comm'n*, 235 Ark. 812, 362 S.W.2d 680 (1962); *Southern Cal. Gas Co.*, 35 PUB. UTIL. REP. (PUR) 3d 300 (Cal. P.U.C. 1960); *Central Me. Power Co. v. Maine Pub. Utils. Comm'n*, 153 Me. 228, 136 A.2d 726 (1957); *State ex rel. Dyer v. Missouri Pub. Serv. Comm'n*, 341 S.W.2d 975 (Mo. 1960).

95. See, e.g., *Southern Cal. Gas Co.*, 35 PUB. UTIL. REP. (PUR) 3d 300 (Cal. P.U.C. 1960); *Kansas City Power & Light Co.*, 6 PUB. UTIL. REP. (PUR) 4th 321 (Kan. State Corp. Comm'n 1974); *Promotional Activities By Gas & Elec. Corps.*, 68 PUB. UTIL. REP. (PUR) 3d 162 (N.Y.P.S.C. 1967).

96. See FEDERAL POWER COMMISSION, THE 1970 NATIONAL POWER SURVEY, pt. 1, ch. 1, at 34 (1971); A. FINDER, *supra* note 2, at 47. For a more detailed treatment of the utility economic growth of this period, see Note, *State Regulation of Advertising by Investor-Owned Electric Utilities: The Development of Current Standards and Their Constitutional Limits*, 12 IND. L. REV. 603, 607-11 (1979). For a discussion of the principle of economies of scale, see notes 23-29 *supra* and accompanying text.

97. See A. FINDER, *supra* note 2, at 47.

98. See *West Ohio Gas. Co. v. Ohio Pub. Utils. Comm'n*, 294 U.S. 63, 72 (1935) ("[w]ithin the limits of reason, advertising or development expenses to foster normal growth are legitimate

icy of promoting growth and consumption. Primarily because of reduced economies of scale,⁹⁹ especially for electric utilities,¹⁰⁰ the expansion oriented policies no longer brought about reduced per unit service costs. Cognizant of these and other developments,¹⁰¹ most regulatory decision makers abandoned the traditional reasonableness standard and began restricting electric and gas utility advertising on the basis of content.¹⁰² By directly prohibiting advertising¹⁰³ and disallow-

charges upon income for rate purposes as for others"); cases cited in notes 94-95 *supra*; Note, *supra* note 96, at 609 & n.45.

99. See A. FINDER, *supra* note 2, at 1. In addition, a reduction in demand growth as well as social and environmental concerns have also contributed to this change in advertising policy. See THE ENERGY SOURCE BOOK, *supra* note 4, at 92; *National Energy Act: Hearings on H.R. 6831, H.R. 687, H.R. 1562, H.R. 2088, H.R. 2818, H.R. 3317, H.R. 3664, H.R. 6660 Before the Subcomm. on Energy and Power of the House Comm. on Interstate and Foreign Commerce, 95th Cong., 1st Sess., pt. 3, vol. 1, at 78-79 (1977) [hereinafter referred to as *National Energy Act Hearings*]; Note, *supra* note 96, at 612.*

100. The decline in efficiency of the economies of scale principle applies primarily to the electric utility industry. See THE ENERGY SOURCE BOOK, *supra* note 4, at 92; Note, *supra* note 96, at 611-12. Because gas and electric utilities have distinctive operating efficiencies, the principle of economies of scale operates more economically for gas utilities today. See Brief for Appellants at 19, 66-67, *Laclede Gas Co. v. Public Serv. Comm'n*, 600 S.W.2d 222 (Mo. Ct. App. 1980), *appeal dismissed*, 449 U.S. 1072 (1981).

101. Since the 1973 Arab oil embargo, the nation and especially public service commissions have developed an acute consciousness for energy conservation. See note 5 *supra*. Closely paralleling the energy shortage has been the rapid acceleration of retail energy costs. See R. PIERCE, G. ALLISON & P. MARTIN, *supra* note 4, at 739; THE ENERGY SOURCE BOOK, *supra* note 4, at 92; Netschert, *supra* note 5, at 17. Accordingly, public service commissions have become even more cost conscious. See Note, *supra* note 10, at 107 n.118.

102. See, e.g., *Arkansas Power & Light Co.*, 15 PUB. UTIL. REP. (PUR) 4th 153 (Ark. P.S.C. 1976); *Los Angeles v. Public Serv. Comm'n*, 7 Cal. 3d 331, 497 P.2d 785, 102 Cal. Rptr. 313 (1972); *Public Serv. Co.*, 13 PUB. UTIL. REP. (PUR) 4th 40 (Colo. P.U.C. 1975); *Tampa Elec. Co.*, 9 PUB. UTIL. REP. (PUR) 4th 402 (Fla. P.S.C. 1975); *In re Hawaiian Elec Co.*, 56 Hawaii 260, 535 P.2d 1102 (1975); *Potomac Elec. Power Co.*, 10 PUB. UTIL. REP. (PUR) 4th 13 (Md. P.S.C. 1975); *Public Serv. Co. v. State*, 113 N.H. 497, 311 A.2d 513 (1973); *Utility Advertising Expenditures*, 14 PUB. UTIL. REP. (PUR) 4th 578 (Or. P.U.C. 1976); *Narragansett Elec. Co.*, 1 PUB. UTIL. REP. (PUR) 4th 60 (R.I.P.U.C. 1973).

This trend has continued. See, e.g., *Re Atlanta Gas Light Co.*, No. 3167-U (Ga. P.S.C. Jan. 19, 1980); *Re Commonwealth Edison Co.*, 35 PUB. UTIL. REP. (PUR) 4th 49 (Ill. Commerce Comm'n 1980); *Re Determination of Whether Advertising Rules Conform to Pub. Util. Regulatory Policies Act of 1978*, No. 35723 (Ind. P.S.C. Jan. 16, 1980); *Re Michigan Gas Util. Co.*, No. U-6022 (Mich. P.S.C. Feb. 5, 1980); *Re Advertising Practices of Tel., Elec. & Gas Distribution Cos.*, 35 PUB. UTIL. REP. (PUR) 4th 361 (N.J. Bd. Pub. Utils. 1980); *Re Gas Co.*, 35 PUB. UTIL. REP. (PUR) 4th 106 (N.M.P.S.C. 1980); *Re Ohio Edison Co.*, 33 PUB. UTIL. REP. (PUR) 4th 435 (Ohio P.U.C. 1980); *Re South Carolina Elec. & Gas Co.*, 34 PUB. UTIL. REP. (PUR) 4th 458 (S.C.P.S.C. 1980); *Re Madison Gas & Elec. Co.*, 34 PUB. UTIL. REP. (PUR) 4th 569 (Wis. P.S.C. 1980).

103. See notes 165-67 *infra* and accompanying text.

ing the allocation of advertising costs in ratemaking proceedings,¹⁰⁴ state¹⁰⁵ and federal¹⁰⁶ decisionmakers have given new meaning to the reasonableness standard. A reasonable advertising expense today must promote energy conservation,¹⁰⁷ environmental policies,¹⁰⁸ or economic prudence.¹⁰⁹

Responding to commission restrictions on advertising, effectuated either by direct prohibition or by denial of cost allocation to the ratemaking formula, public utilities have employed, in addition to their

104. See notes 54-81 *supra* and accompanying text.

105. This policy has been adopted by state regulatory commissions, *see, e.g., Re Determination of Whether Advertising Rules Conform to Pub. Util. Regulatory Policies Act of 1978*, No. 35723 (Ind. P.S.C. Jan. 16, 1980); *Re Michigan Gas Utils. Co.*, No. U-6022 (Mich. P.S.C. Feb. 5, 1980); *Re Madison Gas & Elec. Co.*, 34 PUB. UTIL. REP. (PUR) 4th 569 (Wis. P.S.C. 1980); state supreme courts, *see, e.g., Los Angeles v. Public Service Comm'n*, 7 Cal. 3d 331, 497 P.2d 785, 102 Cal. Rptr. 313 (1972); *In re Hawaiian Elec. Co.*, 56 Hawaii 260, 535 P.2d 1102 (1975); and at least one state legislature, *see, e.g., The Conn. Natural Gas Corp.*, 11 PUB. UTIL. REP. (PUR) 4th 66 (Conn. P.U.C. 1975) (Connecticut legislature giving state regulatory commission permission to disallow all political, institutional, and promotional advertising by gas and electric utilities).

106. Congress adopted this content approach to allowing advertising in enacting Titles I and III of PURPA. See 15 U.S.C. §§ 3201-3211 (Supp. III 1979); 16 U.S.C. §§ 2611-2645 (Supp. III 1979). PURPA divides utility advertising into "promotional," "political," and "other" categories. 16 U.S.C. § 2625 (Supp. III 1979). Promotional and political advertising are expressly forbidden advertising subjects for gas and electric utilities. 15 U.S.C. § 3203(b)(2) (Supp. III 1979); 16 U.S.C. § 2623(b)(5) (Supp. III 1979).

The Supreme Court, perhaps unwittingly, adopted this approach to utility advertising regulation in *Central Hudson Gas & Elect. Corp. v. Public Serv. Comm'n*, 447 U.S. 557 (1980). The Court declared energy conservation to be a substantial state interest worthy of justifying a regulation of utility advertising. *Id.* at 569. See notes 273-76 *supra* and accompanying text.

107. See, *e.g., Promotional Practices of Elec. Utils.*, 8 PUB. UTIL. REP. (PUR) 4th 268 (Fla. P.S.C. 1975); *Re Commonwealth Edison Co.*, 35 PUB. UTIL. REP. (PUR) 4th 49 (Ill. Commerce Comm'n 1980); *Re Determination of Whether Advertising Rules Conform to Pub. Util. Regulatory Policies Act of 1978*, No. 35723 (Ind. P.S.C. Jan. 16, 1980); *Michigan Power Co.*, 18 PUB. UTIL. REP. (PUR) 4th 418 (Mich. P.S.C. 1977); *Re Interstate Power Co.*, 32 PUB. UTIL. REP. (PUR) 4th 494 (Minn. P.S.C. 1979); *Re Advertising Practices of Tel., Elec., & Gas Distribution Cos.*, 35 PUB. UTIL. REP. (PUR) 4th 361 (N.J. Bd. Pub. Utils. 1980); *Re Gas Co.*, 35 PUB. UTIL. REP. (PUR) 4th 106 (N.M.P.S.C. 1980); *Re South Carolina Elec. & Gas Co.*, 34 PUB. UTIL. REP. (PUR) 4th 458 (S.C.P.S.C. 1980).

108. See, *e.g., Pacific Gas & Elec. Co.* 87 PUB. UTIL. REP. (PUR) 3d 270 (Cal. P.U.C. 1971); *Public Serv. Co.*, 13 PUB. UTIL. REP. (PUR) 4th 40 (Colo. P.U.C. 1975); *Promotional Practices of Elec. Utils.*, 8 PUB. UTIL. REP. (PUR) 4th 268 (Fla. P.S.C. 1975); *In re Hawaiian Elec. Co.*, 56 Hawaii 260, 535 P.2d 1102 (1975).

109. Economic concerns include inflation, *see, e.g., Promotional Practices of Elec. Utils.*, 8 PUB. UTIL. REP. (PUR) 4th 268 (Fla. P.S.C. 1975); *Detroit Edison Co.*, 3 PUB. UTIL. REP. (PUR) 4th 209 (Mich. P.S.C. 1974); benefits to the consumer, *see, e.g., Re Interstate Power Co.*, 32 PUB. UTIL. REP. (PUR) 4th 494 (Minn. P.S.C. 1979); *Re Minnesota Gas Co.*, 32 PUB. UTIL. REP. (PUR) 4th 1 (S.D.P.U.C. 1979); and cost control, *see, e.g., Re Gas Co.*, 35 PUB. UTIL. REP. (PUR) 4th 106 (N.M.P.S.C. 1980).

traditional defenses, a new first amendment defense based on the commercial speech doctrine.

II. THE COMMERCIAL SPEECH DOCTRINE

A. *Early Doctrine*

The Supreme Court first confronted the commercial speech doctrine in 1942 in *Valentine v. Chrestensen*.¹¹⁰ In defiance of a New York ordinance banning the streetside distribution of commercial advertising,¹¹¹ Chrestensen distributed handbills that on one side solicited customers to tour his Navy submarine for a fee and on the other side criticized a city ordinance banning his submarine from utilizing city owned docks.¹¹² Police restrained Chrestensen for violating a city commercial handbill ordinance.¹¹³ Chrestensen sought to enjoin the prohibition of handbill distribution on free speech grounds.¹¹⁴ The Court held, without explanation, that the Constitution did not protect commercial speech.¹¹⁵

The Court reinforced this exception doctrine¹¹⁶ for commercial speech in *Breard v. Alexandria*.¹¹⁷ To justify the exception the Court

110. 316 U.S. 52 (1942).

111. The specific ordinance involved in *Valentine* was the New York Sanitary Code, § 318, which provides in pertinent part: "No person shall . . . distribute, or cause . . . to be . . . distributed, any handbill, circular, . . . or other advertising matter whatsoever in or upon any street or public place. . . . This section is not intended to prevent the lawful distribution of anything other than commercial and business advertising matter." 316 U.S. at 53 n.1.

112. *Id.* at 53.

113. *Id.*

114. *Id.* at 54. Although Chrestensen sought relief under the fourteenth amendment, the Supreme Court framed the issue in terms of "whether the ordinance . . . was . . . an unconstitutional abridgement of the freedom of . . . speech." *Id.*

115. Justice Roberts concluded:

This court has unequivocally held that the streets are proper places for the exercise of the freedom of communicating information . . . and municipalities may . . . not unduly burden or proscribe its employment in these public thoroughfares. We are equally clear that the Constitution imposes no such restraint on government as respects purely commercial advertising.

Id.

For a criticism of the conclusory nature of the *Valentine* opinion, see Farber, *Commercial Speech and First Amendment Theory*, 74 NW. U.L. REV. 372, 377 (1979); Heller, *The End of the "Commercial Speech" Exception—Good Riddance or More Headaches For the Courts?*, 67 KY. L. REV. 927, 927-36 (1979).

116. Commentators have labeled the commercial speech exception to the first amendment's general protection of speech as the "exception doctrine." See, e.g., Heller, *supra* note 115, at 927-30.

117. 341 U.S. 622 (1951). In *Breard*, the Court upheld a city ordinance banning door-to-door

cited the commercial speaker's profit motive as the distinguishing factor for denying commercial speech the full first amendment protection accorded other types of speech.¹¹⁸

After *Breard*, the Supreme Court did not address the commercial speech issue again until the late 1960s.¹¹⁹ Toward the end of this period, a concept referred to as the "right to know"¹²⁰ warranted the at-

solicitation for magazine subscriptions. *Id.* at 645. *Chrestensen* and *Breard* have since been cited as denying all protection to commercial speech. See L. TRIBE, *AMERICAN CONSTITUTIONAL LAW* 653 n.16 (1978).

118. In upholding the ordinance, the Court distinguished *Martin v. City of Struthers*, 319 U.S. 141 (1943), in which the Court had struck down an ordinance forbidding the free distribution of advertisements of religious meetings. *Id.* at 146-47. After comparing the differences between the commercial nature of the magazine solicitations in *Breard* and the religious nature of the handbill distribution in *Martin*, Justice Reed concluded that the two cases should be distinguished: "As no element of the commercial entered into [*Martin*] . . . and the opinion was narrowly limited to the precise fact of the free distribution of an invitation to religious services, we feel that it is not necessarily inconsistent with the conclusion reached in this case." 341 U.S. at 643. For a discussion of the purported economic justification for the commercial speech exception, see *Heller*, *supra* note 115, at 928-30.

Even though the Court sought to rest the justification for the exception doctrine on the grounds of profit motive, the Court nevertheless in subsequent decisions approved first amendment protection for other profit motivated media activities. See *New York Times v. Sullivan*, 376 U.S. 254 (1964) (newspaper print advertisements); *Smith v. California*, 361 U.S. 147 (1959) (books); *Joseph Burstyn, Inc. v. Wilson*, 343 U.S. 495 (1952) (movies). See also Note, *Commercial Speech—An End in Sight for Chrestensen?*, 23 DEPAUL L. REV. 1258 (1974). The contradictory nature of the *Valentine-Breard* exception doctrine and the Court's subsequent treatment of economic motive cases prompted one commentator to describe the status of commercial speech under the first amendment to be in a "chaotic state." T. EMERSON, *THE SYSTEM OF FREEDOM OF EXPRESSION* 16 (1970).

119. Until 1973 the Supreme Court considered the commercial speech exception only in passing. See *New York Times Co. v. Sullivan*, 376 U.S. 254 (1964). In *New York Times*, the Court, upholding first amendment protection for a libelous political advertisement, distinguished *Chrestensen* on the basis that the *New York Times* advertisement was injected with political overtones, whereas *Chrestensen* "was based upon the factual conclusions that the handbill was 'purely commercial advertising.'" *Id.* at 266.

During this same period, lower courts confirmed the commercial speech exception doctrine. See *Pollack v. Public Util. Comm'n*, 191 F.2d 450, 457 (D.C. Cir. 1951), *rev'd on other grounds*, 343 U.S. 451 (1953); *Halstead v. SEC*, 182 F.2d 660, 668 (D.C. Cir. 1950).

The Supreme Court recognized the commercial speech hiatus as well in *Virginia State Bd. of Pharmacy v. Virginia Citizens Consumer Council*, 425 U.S. 748 (1976). "Since the decision in *Breard* . . . the Court has never denied protection on the ground that the speech in issue was 'commercial speech.'" *Id.* at 759.

120. This concept may also be referred to as the "right to receive." See *Heller*, *supra* note 115, at 931; Comment, *The Right to Receive and the Commercial Speech Doctrine: New Constitutional Considerations*, 63 GEO. L.J. 775 (1975). The "right to know" has been defined as "a right to receive information communicated by another." See Note, *Attorneys' Rights Under the Code of Professional Responsibility: Free Speech, Right to Know and Freedom of Association*, 1977 WASH.

tion of constitutional commentators¹²¹ and some members of the Court.¹²² This concept fostered the eventual change in thought that favored first amendment protection of commercial speech.¹²³

The change came in *Virginia State Board of Pharmacy v. Virginia Citizens Consumer Council*,¹²⁴ in which the Court based its decision on a "right to know" concept and held that even purely commercial speech was entitled to some first amendment protection.¹²⁵ The *Virginia State*

U.L.Q. 682, 706. See generally 26 DEPAUL L. REV. 134 (1976); 13 SUFFOLK U.L. REV. 1503 (1979); 16 WASHBURN L. REV. 197 (1976).

121. The concept of "right to know" in the first amendment context may be traced to *Martin v. City of Struthers*, 319 U.S. 141 (1943), in which the Court stated that "freedom of speech necessarily protects the right to receive [speech]." *Id.* at 143.

Professor Meikeljohn justified the "right to know" concept as an incident to the "market place of ideas." A. MEIKELJOHN, *FREE SPEECH AND ITS RELATION TO SELF-GOVERNMENT* (1948). See Emerson, *Legal Foundations of the Right to Know*, 1976 WASH. U.L.Q. 1. In order for the "marketplace of ideas" to function properly, recipients of those ideas need protection. See *Heller*, *supra* note 115, at 931.

The notion of the "marketplace of ideas" was first expressed judicially by Justice Holmes in *Abrams v. United States*, 250 U.S. 616, 630 (1919). For a skeptical view of the utility of the marketplace of ideas concept, see Baker, *Scope of the First Amendment Freedom of Speech*, 25 U.C.L.A. L. REV. 964, 967-81 (1978).

122. See *Griswold v. Connecticut*, 381 U.S. 479, 482 (1965); *Lamont v. Postmaster Gen.*, 381 U.S. 301, 308 (1965) (Brennan, J., concurring); *Martin v. City of Struthers*, 319 U.S. 141, 143 (1943). The Court formally acknowledged this concept as constitutionally viable in 1969 by stating, "It is now well established that the constitution protects the right to receive information and ideas." *Stanley v. Georgia*, 394 U.S. 557, 564 (1969).

123. In *Pittsburgh Press v. Human Relations Comm'n*, 413 U.S. 376 (1973), a decision reaffirming the holding in *Valentine*, tensions surfaced between the *Valentine* commercial speech exception and the "right to know" concept. The *Pittsburgh Press* Court, which affirmed *Valentine's* denial of first amendment protection for commercial speech, decided the case by a 5-4 margin. Four justices lodged strong dissents. *Id.* at 393-404 (Burger, C.J., & Douglas, Stewart, and Brennan, J.J., dissenting). Moreover, one of the dissenters called for the outright demise of the *Valentine* commercial speech exception. *Id.* at 397-98 (Douglas, J., dissenting). The close outcome in *Pittsburgh Press* indicated that some members of the Court had reevaluated their views regarding commercial speech protection.

Two years after *Pittsburgh Press*, four justices expressed doubt as to the validity of the commercial speech exception in *Bigelow v. Virginia*, 421 U.S. 809 (1975), an abortion advertising case. At that point, with five justices willing to overrule the commercial speech exception, the fall of *Valentine* was imminent.

124. 425 U.S. 748 (1976).

125. *Id.* at 773. The Court, per Justice Blackmun, stated:

[T]he free flow of commercial information[, e]ven an individual advertisement, though entirely "commercial," may be of general public interest. . . . Advertising . . . is . . . dissemination of information It is a matter of public interest that those decisions, in the aggregate, be intelligent and well informed. To this end, the free flow of commercial information is indispensable.

Id. at 764-65. See generally Alexander, *Speech in the Local Marketplace: Implications of Virginia State Board of Pharmacy v. Virginia Citizens Consumer Council, Inc. for Local Regulatory Power*,

Board plaintiffs, consumers of prescription drugs, challenged a Virginia statute¹²⁶ prohibiting pharmacists from advertising prices of prescription drugs.¹²⁷ In protecting commercial speech by striking down the statute, the Court nevertheless stopped short of extending full first amendment protection to commercial speech by specifically mentioning two commercial speech areas in which it would accord no first amendment protection whatsoever.¹²⁸ The Court failed to delineate fully the extent to which the decision does provide protection.

Post-*Virginia State Board* commercial speech cases¹²⁹ indicate that different forms of commercial speech receive varying degrees of protection.¹³⁰ These distinctions are primarily a function of three overriding concerns articulated by the Court. One concern focused on honoring the common sense differences between commercial and noncommercial speech.¹³¹ Another concern was fear of diluting the protection for "pure speech"¹³² by treating commercial speech and noncommercial

14 SAN DIEGO L. REV. 357 (1977); Elman, *The New Constitutional Right to Advertise*, 64 A.B.A.J. 206 (1978); Comment, *First Amendment Protection for Commercial Advertising: The New Constitutional Doctrine*, 44 U. CHI. L. REV. 205 (1976).

126. The challenged Virginia statute stated in pertinent part: "Any pharmacist shall be considered guilty of unprofessional conduct who . . . publishes, advertises, or promotes . . . any amount, price, fee, premium, discount, rebate or credit terms for professional services or for drugs containing narcotics or for any drugs which may be dispensed only by prescription." VA. CODE § 54-524.35 (1974) (current version Cum. Supp. 1981).

127. 425 U.S. at 749-50.

128. The forms of permissible regulation the Court mentioned were reasonable time, place, and manner restrictions and restrictions on untruthful, deceptive, or misleading speech. *Id.* at 771.

129. *Central Hudson Gas & Elec. Co. v. Public Serv. Comm'n*, 447 U.S. 557 (1980); *Consolidated Edison Co. v. Public Serv. Comm'n*, 447 U.S. 530 (1980); *Friedman v. Rogers*, 440 U.S. 1 (1979); *Ohralik v. Ohio State Bar Ass'n*, 436 U.S. 447 (1978); *First Nat'l Bank of Boston v. Bellotti*, 435 U.S. 765 (1978); *In re Primus*, 436 U.S. 412 (1978); *Bates v. State Bar*, 433 U.S. 350 (1977); *Carey v. Population Servs. Int'l*, 431 U.S. 678 (1977); *Linmark Assocs., Inc. v. Township of Willingboro*, 431 U.S. 85 (1977).

130. See Note, *Restrictions on Electric Utility Advertising*, 78 MICH. L. REV. 433, 435 (1980).

131. See *Ohralik v. Ohio State Bar Ass'n*, 436 U.S. 447, 455-56 (1978); *Linmark Assocs., Inc. v. Township of Willingboro*, 431 U.S. 85, 98 (1977); *Virginia State Bd. of Pharmacy v. Virginia Citizens Consumer Council*, 425 U.S. 748, 771 n.24 (1976). The Court in *Ohralik* noted: "We have not discarded the 'common sense' distinction between speech proposing a commercial transaction, which occurs in an area traditionally subject to government regulation, and other varieties of speech." 436 U.S. at 455-56. See generally Note, *supra* note 130.

132. "Pure speech" as used in this context is that speech which is noncommercial. Pure speech, or speech that is noncommercial, is generally accorded a preferred position enjoying the full panoply of first amendment protection. Thus, in order for infringements on such speech to be justified, a "compelling," "significant," or "important" governmental interest must be shown. See, e.g., *Erznoznik v. City of Jacksonville*, 422 U.S. 205, 217 (1975); *Grayned v. City of Rockford*, 408

speech on constitutional parity.¹³³ Finally, the Court explained that commercial speech, due to its economic motivation, is more durable and less likely to be "chilled" than noncommercial speech.¹³⁴ Motivated by these concerns, the Court developed a two-tiered approach for protection of commercial speech: commercial speech that is related to regulatable governmental activity is more amenable to control,¹³⁵ while commercial speech not related to an area of regulatable governmental activity is accorded more traditional first amendment protection.¹³⁶

U.S. 104, 115 (1972); NAACP v. Button, 371 U.S. 415, 438 (1963). Nevertheless, pure speech in certain instances may be regulated without a showing of constitutional significance. As defined in Chaplinsky v. New Hampshire, 315 U.S. 568 (1942), the following classes of speech may be fully subjected to government regulation: "These include the lewd and obscene, the profane, the libelous, and the insulting or 'fighting' words . . ." *Id.* at 572.

Because commercial speech is not accorded the same status as "pure speech," principles developed in the traditional first amendment context "do not extend automatically to this as yet uncharted area." *Friedman v. Rogers*, 440 U.S. 1, 11 n.9 (1979). Hence, "overbreadth" analysis and protection against "prior restraints" are unavailable to commercial speech. *See Ohralik v. Ohio State Bar Ass'n*, 436 U.S. 447, 462 n.20 (1978) (overbreadth not available); *Virginia State Bd. of Pharmacy v. Virginia Citizens Consumer Council*, 425 U.S. 748, 772 n.24 (1976) (no protection against prior restraints).

133. *Ohralik v. Ohio State Bar Ass'n*, 436 U.S. 447, 456 (1978). The Court declared: "To require a parity of constitutional protection for commercial and non-commercial speech alike could invite dilution, simply by a leveling process, of the force of the Amendment's guarantee with respect to the latter kind of speech." *Id. Accord*, *Central Hudson Gas & Elec. Co. v. Public Serv. Comm'n*, 447 U.S. 557, 562-63 n.5 (1980) (commercial expression is of less constitutional significance than other forms of speech). *See generally* Note, *supra* note 130.

134. The Court in *Virginia State Board* stated: "Commercial speech may be more durable than other kinds. Since advertising is the *sine qua non* of commercial profits, there is little likelihood of its being chilled by proper regulation and forgone entirely." 425 U.S. at 771-72 n.24. *See generally* Note, *supra* note 130.

135. *See Farber, supra* note 115, at 386-87; Jackson & Jeffries, *Commercial Speech: Economic Due Process and the First Amendment*, 65 VA. L. REV. 1, 38-39 (1979); Note, *supra* note 130, at 436, 438. *See also In re Primus*, 436 U.S. 412 (1978), in which an ACLU attorney advised a group of sterilized women of their legal rights against the federal government. As a result of the meeting, the attorney subsequently informed one of the women of the availability of free ACLU legal assistance. The Disciplinary Board of the South Carolina Supreme Court reprimanded the attorney. In declaring that South Carolina's application of its disciplinary rules violated the attorney's first amendment rights, the Court distinguished *Primus* from *Ohralik v. Ohio State Bar Ass'n*, 436 U.S. 447 (1978), on the grounds of regulatable governmental activity:

Normally the purpose or motive of the speaker is not central to First Amendment protection but it does bear on the distinction between conduct that is "an associational aspect of 'expression' " . . . and *other activity subject to plenary regulation by government* In *Ohralik* . . . the lawyer was not engaged in associational activity for the advancement of beliefs and ideas; his purpose was the advancement of his own commercial interests.

In re Primus, 436 U.S. at 438 n.32 (emphasis added).

136. When the commercial speech is related to more fundamental constitutional rights not subject to government regulation, the Court will be inclined to accord traditional first amendment

Post-*Virginia State Board* decisions concerning regulatable commercial speech clarified the doctrine. Subsequent decisions,¹³⁷ for example, reaffirmed the policy to which the Court alluded in pre-*Virginia State Board* decisions¹³⁸ that false or misleading commercial speech is not constitutionally protected.¹³⁹ Furthermore, the state's interest, when balanced against the interests of commercial speech, must be substantial.¹⁴⁰ In addition, under *Bates v. State Bar*,¹⁴¹ the state's legislation must have a direct causal connection to its asserted interest¹⁴² and must further the interest in a reasonable manner.¹⁴³ Accordingly, a state

protection. See Note, *supra* note 130, at 438. See also *Carey v. Population Servs. Int'l*, 431 U.S. 678 (1977) (Court upheld a right to privacy in striking down a statute prohibiting advertisement of contraceptives); *Linmark Assocs., Inc. v. Township of Willingboro*, 431 U.S. 85 (1977) (Court, employing a right to travel rationale, declared unconstitutional an ordinance forbidding the display of residential "For Sale" signs); *Bigelow v. Virginia*, 421 U.S. 809 (1975) (Court invalidated a Virginia statute prohibiting New York abortion advertisements because the citizens of Virginia had a right to travel to New York and privacy issues were involved).

137. See *Friedman v. Rogers*, 440 U.S. 1 (1979); *Ohralik v. Ohio State Bar Ass'n*, 436 U.S. 447 (1978). See also *Virginia State Bd. of Pharmacy v. Virginia Citizens Consumer Council*, 425 U.S. 748, 771, 772 n.24 (1976), in which the Court stated that "[u]ntruthful speech, commercial or otherwise, has never been protected for its own sake We foresee no obstacle to a State's dealing effectively with this problem." *Id.* at 771 (citations omitted).

In *Friedman*, the Court upheld a ban restricting optometrists' use of trade names that the Court found could mislead the public as to the source and quality of the optometric service. The Court declared that "it is clear that the state's interest in protecting the public from the deceptive and misleading use of optometrical trade names is substantial and well demonstrated." 440 U.S. at 15.

In *Ohralik*, the Court upheld an Ohio State Bar Association rule that prohibited in-person solicitation of clients. The Court determined that the potentiality for deception created by the untrained at the hands of a "professional" counselor and persuader was too great to go unchecked. 436 U.S. at 464-65. See also *Farber, supra* note 121, at 384-95.

138. See *Bigelow v. Virginia*, 421 U.S. 809, 821 (1975); *Pittsburgh Press Co. v. Pittsburgh Comm'n on Human Relations*, 413 U.S. 376, 389 (1973). The Court in *Pittsburgh Press* stated that "[a]ny First Amendment interest which might be served by advertising an ordinary commercial proposal and which might arguably outweigh the governmental interest supporting the regulation is altogether absent when the commercial activity itself is illegal and . . . incidental to a valid limitation on economic activity." *Id.* at 389 (emphasis added).

139. 425 U.S. at 766-70.

140. See, e.g., *Friedman v. Rogers*, 440 U.S. 1, 15 (1979) (state's interest in protecting public from deceptive and misleading use of trade names is a substantial one); *Ohralik v. Ohio State Bar Ass'n*, 436 U.S. 458, 462 (1978) (State's interest in protecting public from attorney solicitation legitimate and important).

141. 433 U.S. 350 (1978).

142. *Id.* at 378. In *Bates*, the Court confronted the legality of an Arizona State Bar Association rule that prohibited price advertising by attorneys. In extending first amendment protection to the newspaper advertisements for routine legal services, the Court determined that the regulation was only remotely related to the asserted state interest of prohibiting unprofessional conduct. *Id.* at 382.

143. The *Virginia State Board* Court concluded that a complete suppression of "concededly

may use only those means necessary to effectuate its goals; if possible, a state should invoke less inhibiting regulation.

B. *The Central Hudson Test*

The Court crystallized *Virginia State Board* and its subsequent clarifications into a formal test in *Central Hudson Gas & Electric Co. v. Public Service Commission*.¹⁴⁴ In *Central Hudson*, the New York Public Service Commission had imposed a promotional advertising ban originally in response to the 1973 Arab oil embargo and the resultant energy crisis.¹⁴⁵ When the Commission extended the ban after the energy crisis abated, Central Hudson Gas & Electric challenged the ban on first amendment grounds.¹⁴⁶ Deciding in favor of Central Hudson, the Court established a four-part test for balancing a utility's right to commercial speech against a governmental regulation prohibiting such speech.¹⁴⁷

Rooted in *Virginia State Board* and its progeny,¹⁴⁸ the four-part analysis focuses on the governmental interest that the regulation is to

truthful information about [an] entirely lawful activity" was too sweeping in nature. 425 U.S. at 773. In subsequent cases this concept was given further consideration. In *In re Primus*, 436 U.S. 412 (1978), the Court held that the "state's . . . interest in regulating members [whose] profession it licenses . . . amply justifies the application of narrowly drawn rules to proscribe solicitation . . ." *Id.* at 438 (emphasis added).

144. 447 U.S. 557 (1980). After discussing the doctrinal history of commercial speech, the Court enunciated a four-part test:

In commercial speech cases, then, a four-part analysis has developed. At the outset, we must determine whether the expression is protected by the First Amendment. For commercial speech to come within that provision, it at least must concern lawful activity and not be misleading. Next, we ask whether the asserted governmental interest is substantial. If both inquiries yield positive answers, we must determine whether the regulation directly advances the governmental interest asserted, and whether it is not more extensive than is necessary to serve that interest.

Id. at 566. See notes 151-55 *infra* and accompanying text.

145. See Notice of Proposal, *supra* note 5, at 2074-76. The Commission, in determining that the "demands for electrical energy . . . cannot be met for the foreseeable future without significant reductions in usage in view of the lack of sufficient fuels to generate electricity," ordered the electric utilities of New York to discontinue "promoting the use of electricity through advertising . . ." *Id.* at 2072, 2076.

146. Before the decision to extend the ban, the Public Service Commission in July 1976 solicited public opinion on the promotional advertising ban issued three years earlier. After hearing arguments from opponents and proponents of the ban, the Commission reaffirmed the ban in February 1977. See Statement on Policy on Advertising and Promotional Practices of Public Utilities, 17 N.Y. PSC 2-R, 3-R (Feb. 25, 1977).

147. 447 U.S. at 566.

148. The Court disapproved of the "complete suppression of Central Hudson's advertising." *Id.* at 571.

serve and the means employed to achieve that interest.¹⁴⁹ The *Central Hudson* test, as a practical matter, consists of five parts, because a court must make an initial decision as to whether the speech at issue is indeed commercial.¹⁵⁰

If a court determines that the speech is commercial, the first step is for the court to decide whether the speech is either "misleading or related to the unlawful."¹⁵¹ If the speech falls within either of those categories, the court can properly validate the government regulation. If the speech is not within the categories, the second part of the test requires the state to show a substantial interest in promulgating the regulation.¹⁵² The third part of the test requires an analysis of whether the asserted state interest is directly effectuated by the regulatory means.¹⁵³ The fourth part requires that the state's regulatory means restrict advertising no more than necessary.¹⁵⁴ If a state regulation satisfies each element of the test, the regulation is immune to a first amendment commercial speech defense.¹⁵⁵

Although the *Central Hudson* test is relatively new, courts have already employed it in several commercial speech defense cases.¹⁵⁶ Recently, utilities have invoked this defense when challenging advertising

149. See notes 124-43 *supra* and accompanying text.

150. The Court provided: "At the outset, we must determine whether the expression is protected by the first amendment." 447 U.S. at 566. The traditional definition of commercial speech is that which does no more than propose a commercial transaction." *Virginia State Bd. of Pharmacy v. Virginia Citizens Consumer Council*, 425 U.S. 748, 771 n.24 (1976). The Court in *Central Hudson* expanded the notion of commercial speech by defining it as "expression related solely to the economic interests of the speaker and its audience." 447 U.S. at 561.

If the speech in question qualifies as commercial, the *Central Hudson* test must be used to evaluate it. If, on the other hand, the speech is noncommercial, and thus fully protected, the speech will be evaluated on traditional first amendment grounds. See note 132 *supra*.

151. *Friedman v. Rogers*, 440 U.S. 1 (1979). See *Ohralik v. Ohio State Bar Ass'n*, 436 U.S. 447 (1978); *Virginia State Bd. of Pharmacy v. Virginia Citizens Consumer Council*, 425 U.S. 748 (1976). See notes 137-38 *supra* and accompanying text.

152. See notes 140-43 *supra* and accompanying text.

153. See *Bates v. State Bar*, 433 U.S. 350 (1977); *Virginia State Bd. of Pharmacy v. Virginia Citizens Consumer Council*, 425 U.S. 748 (1976). See note 142 *supra* and accompanying text.

154. See *In re Primus*, 436 U.S. 412 (1978); *Bates v. State Bar*, 433 U.S. 350 (1977); *Carey v. Population Servs. Int'l*, 431 U.S. 678 (1977); *Virginia State Bd. of Pharmacy v. Virginia Citizens Consumer Council*, 425 U.S. 748 (1976). See note 143 *supra* and accompanying text.

155. 447 U.S. at 570-71.

156. See, e.g., *Metromedia, Inc. v. City of San Diego*, 101 S. Ct. 2882 (1981); *Record Revolution No. 6, Inc. v. Parma*, 638 F.2d 619 (6th Cir. 1980); *Equifax Servs., Inc. v. Cohen*, 420 A.2d 189 (Me. 1980), *cert. denied*, 450 U.S. 916 (1981); *State v. Miller*, 83 N.J. 402, 416 A.2d 821 (1980). See also *Massena v. Niagra Mohawk Power Corp.*, No. 79-CV-163 (S.D.N.Y. Sept. 8, 1981).

restrictions.¹⁵⁷

III. ANALYSIS OF ADVERTISING REGULATIONS UNDER *CENTRAL HUDSON*

Public service commissions can regulate utility advertising by directly prohibiting the advertising¹⁵⁸ or by disallowing allocation of the advertising expense to the rate schedule.¹⁵⁹ In response to both types of regulation, a utility may invoke the first amendment commercial speech defense.¹⁶⁰ The advantages and viability of this defense will

157. See, e.g., *Central Hudson Gas & Elec. Co. v. Public Serv. Comm'n*, 447 U.S. 557 (1980); *Laclede Gas Co. v. Public Serv. Comm'n*, 600 S.W.2d 222 (Mo. Ct. App. 1980), *appeal dismissed*, 449 U.S. 1072 (1981); *Rochester Gas & Elec. Corp. v. Public Serv. Comm'n*, 51 N.Y.2d 823, 413 N.E.2d 359, 433 N.Y.S.2d 420 (1980), *appeal dismissed*, 450 U.S. 961 (1981).

158. See notes 163-95 *infra* and accompanying text.

159. See notes 196-271 *infra* and accompanying text. For purposes of this Note, "rate schedule" refers to the inclusion of certain advertising expenses in the revenue formula discussed at notes 71-85 *supra* and accompanying text. The effect of including an expenditure in the rate schedule is to pass that cost on to the consumer in the form of customer rates. See *id.* The term "rate base" should not be used synonymously with the term "rate schedule," "revenue formula" or "consumer charge." "Rate base" is a technical term of art used in the ratemaking process. The rate base is the formula that expresses the *Smyth* "fair value" requirement and is defined to be the sum of the utility's original investment and the working capital allowance less accumulated depreciation. See notes 74-77 *supra* and accompanying text. Members of the Supreme Court apparently indiscriminately used this term in *Consolidated Edison Co. v. Public Serv. Comm'n*, 447 U.S. 530, 543 (1980); *id.* at 544 (Marshall, J., concurring).

160. See note 12 *supra* and accompanying text.

Indeed, some argue that the first amendment is the only plausible defense available to utilities in this context. Those who make this assertion argue that the traditional defenses of due process and undue assault on management prerogative, see note 10 *supra*, are no longer valid. See Note, *supra* note 96, at 623. Those who espouse this theory correctly point out that the "current conditions . . . [produce] the dilemmas of demand growth and rising costs in . . . the power industry." *Id.* This situation differs considerably from the status of utilities during the *West Ohio Gas* era.

West Ohio Gas was decided under a fourteenth amendment due process analysis. 294 U.S. at 71. Fourteenth amendment due process "demands . . . that the law shall not be unreasonable, arbitrary or capricious, and that the means selected shall have a real and substantial relation to the object sought to be attained." *Nebbia v. New York*, 291 U.S. 502, 525 (1934). The Supreme Court liberalized this analysis in a later opinion by allowing the means to bear only a "rational relation" to the desired end. See *United States v. Carolene Prods. Co.*, 304 U.S. 144, 153-54 (1938). *Accord*, *Williamson v. Lee Optical Co.*, 348 U.S. 483, 491 (1955). In *West Ohio Gas*, the Court determined that the Ohio Public Service Commission did not satisfy the "rational relation" test in attempting to disallow advertising expenses from being passed on to consumers in the form of service rates. The Court rightfully feared that the disallowance of advertising costs would inhibit the "normal growth" of utilities. 294 U.S. at 72. During this period of economic history, continued growth was essential to maintain the financial fitness of the utility so that it could meet the burgeoning energy needs of its customers. See notes 91-98 *supra* and accompanying text. Hence, unless the advertising expenses were unjustifiably excessive, a determination by a public

vary depending upon the scope of regulation,¹⁶¹ the category of advertising,¹⁶² and whether the speaker is a gas or electric utility.

A. *Direct Prohibition*

Typically, public service commissions effectuate direct prohibitions on utility speech by issuing policy statements.¹⁶³ Regardless of the category of advertising¹⁶⁴ or the type of utility-speaker,¹⁶⁵ a defense under the commercial speech doctrine is likely to succeed if the direct prohibition imposes a total ban on speech.

The Supreme Court in *Central Hudson* struck down a total prohibition on promotional advertising.¹⁶⁶ Applying the four-part analysis established in that opinion, the Court reasoned that the Public Service Commission of New York failed to show that its total prohibition of promotional advertising was no more extensive than necessary to achieve the asserted state interest.¹⁶⁷ Although the Court recognized New York's legitimate interest in conserving energy in the wake of the

service commission prohibiting those expenses from being passed on to the consumers as a valid operating expense would violate the rational relation standard.

In the current context, the need for uninhibited expansion no longer exists: energy conservation is now a primary concern; the efficiencies of the "economies of scale" have waned; and the increase in demand is proceeding at a slower rate. See notes 91-101 *supra* and accompanying text. This situation provides an impetus for some to conclude that a rational basis does exist for a regulation denying the cost of advertising expenses to be passed on to consumers. See Note, *supra* note 96, at 612, 623. Accordingly, this conclusion renders a fourteenth amendment due process defense largely impotent in providing a justification for advertising cost allocation by utilities. *Id.* An analysis of whether or not the foregoing argument is valid is beyond the scope of this Note. The mere spectre of doubt raised by this argument, however, underscores the importance of the first amendment defense for utilities.

161. Public service commissions regulate utility advertising by direct prohibition, see notes 163-95 *infra* and accompanying text, and by denial of cost allocation of advertising expenses to consumer rates, see notes 196-271 *infra* and accompanying text.

162. See notes 82-88 *supra* and accompanying text.

163. See, e.g., Notice of Proposal, *supra* note 5, at 2074-76 (ordering discontinuance of "promoting the use of electricity through advertising").

164. The various types of advertising engaged in by a utility include promotional, political, informational, and instructional. For a complete discussion of these categories of advertising, see notes 3 & 82-88 *supra* and accompanying text.

165. Whether the speaker is an electric utility, as opposed to a gas utility, may affect the validity of a commercial speech defense. For a discussion of the import of the electric-gas distinction, see notes 234-72 *infra* and accompanying text.

166. 447 U.S. 557 (1980). Promotional advertising may be defined as "advertising which is designed to obtain new customers, increase usage by present customers, or to encourage customers to select and install appliances using one form of energy in preference to another." PUB. UTIL. FORT., Mar. 1, 1973, at 47. See note 88 *supra* and accompanying text.

167. 447 U.S. at 569-70.

1973 Arab oil embargo, the majority feared the prohibition's broad language would sweep within its ambit other speech that the Commission had not intended to regulate.¹⁶⁸

Similarly, *Consolidated Edison Co. v. Public Service Commission*¹⁶⁹ and *First National Bank of Boston v. Bellotti*¹⁷⁰ struck down total bans on political advertising.¹⁷¹ In *Consolidated Edison*, the New York Public Service Commission issued a policy statement forbidding utilities to discuss political matters in bill inserts.¹⁷² The order directly affected Con-Ed's practice of including pronuclear power inserts in its billing envelopes.¹⁷³ The Commission's ban, however, did not extend to inserts discussing "non-controversial" subjects.¹⁷⁴ Presented with this overt instance of content regulation,¹⁷⁵ the Court found that the policy statement impermissibly infringed on the utility's first amendment rights.¹⁷⁶

168. *Id.* at 570.

169. *Id.* at 530.

170. 435 U.S. 765 (1978).

171. For a definition of political advertising, see notes 86-87 *supra* and accompanying text.

172. On February 17, 1977, the New York Public Service Commission issued a statement prohibiting "utilities from using bill inserts to discuss political matters, including the desirability of future development of nuclear power." 447 U.S. at 532.

173. *Id.*

174. *Id.* The Court noted that the Commission openly admitted that its order discriminated between types of speech content:

The Commission does not pretend that its action is unrelated to the content or subject matter of bill inserts. Indeed, it has undertaken to suppress certain bill inserts precisely because they address controversial issues of public policy. The Commission allows inserts that present information to consumers on certain subjects, such as energy conservation measures, but it forbids the use of inserts that discuss public controversies.

Id. at 537.

175. The Court, in assessing the Commission's reasoning for implementing the ban, declared: "The Commission's own rationale demonstrates that its action cannot be upheld as a content-neutral time, place, or manner regulation." *Id.*

176. *Id.* at 554. *Accord*, Vermont Pub. Interest Research Group, Inc. v. Central Vt. Pub. Serv. Corp., 39 PUB. UTIL. REP. (PUR) 4th 59, 74 (Vt. Pub. Serv. Corp. 1981) (citing *Consolidated Edison* in rejecting and denoting a nuclear power bill insert content regulation as a pervasive form of censorship).

In *Consolidated Edison*, Justice Blackmun, joined by Justice Rehnquist, dissented from the majority's position and embraced the New York Public Service Commission's argument that the "use of the billing envelope to distribute management's pamphlets amount[ed] to a forced subsidy of the utility's speech by the ratepayers." *Id.* at 551. Justice Blackmun suggested that the compulsion of ratepayers to finance a utility's advertising might violate the ratepayers' first and fourteenth amendment rights. *Id.* at 552 n.1 (citing *Abood v. Detroit Bd. of Educ.*, 431 U.S. 209 (1977)).

Justice Marshall, in a concurring opinion, made special note of the fact that the court limited its analysis to the issue of prohibition of speech and in no way attempted to resolve the more difficult

In *Bellotti*, the Massachusetts legislature had passed a statute prohibiting corporate political contributions or expenditures.¹⁷⁷ The state designed the law to prevent corporations from influencing the outcome of referendum proposals. First National Bank of Boston challenged the statute on first amendment grounds.¹⁷⁸ Reasoning that the right to speak on public issues should not turn on the source speaking,¹⁷⁹ the Court held that the statute regulated content and thus violated the first amendment.¹⁸⁰ The Court's decision rested on its determination that the state failed to show a "compelling" interest achieved by a precisely drawn means.¹⁸¹

In both *Bellotti* and *Consolidated Edison*, the majority declined to invoke the commercial speech doctrine and instead based its decision on traditional first amendment grounds.¹⁸² By not deciding these cases under the more lenient commercial speech standard, the Court demonstrated a willingness to provide greater protection for politically oriented advertising. Despite the commercial nature of the speakers, the Court's result was correct because the content of the speech was non-commercial. Accordingly, a court must evaluate a state's total prohibition of a utility's political advertising under the narrower compelling state interest standard.¹⁸³ This stricter standard¹⁸⁴ will cause a direct

issue of whether a "Commission may exclude the costs of bill inserts from the rate base . . ." 447 U.S. at 544. The Commission, however, in denying a petition for rehearing in this case, noted that it would ban these bill inserts even when paid for by the shareholders because, regardless of the financial impetus, the use of inserts in a billing envelope made consumers "a captive audience." *Id.* at 543. Whether requiring shareholders to finance the costs of inserts would otherwise place a damper on utility speech remains an unresolved issue. Justice Blackmun, in his *Consolidated Edison* dissent, argued that "due to the greater likelihood that a recipient would read an insert with the bill, the utility well might desire to place its insert with the bill even if the total cost of the mailing were charged to the shareholders." *Id.* at 554 n.4 (citing Long Island Lighting Co. v. New York Pub. Serv. Comm'n, No. 77 C 972 (E.D.N.Y. Mar. 30, 1979)).

177. MASS GEN. LAWS ANN. ch. 55, § 8 (West Supp. 1977) specifically prohibited corporations from making contributions "for the purpose of . . . influencing or affecting the vote on any question submitted to the voters, other than the one materially affecting any of the property, business or assets of the corporation."

178. 435 U.S. at 770.

179. *Id.* at 777. The Bank wanted to make expenditures to publicize its opposition to a proposed Massachusetts constitutional amendment imposing a graduated income tax upon private individuals. *Id.* at 769.

180. *Id.* at 785.

181. *Id.* at 786.

182. See *Consolidated Edison Co. v. Public Serv. Comm'n*, 447 U.S. 530, 533-34 (1980); *First Nat'l Bank of Boston v. Bellotti*, 435 U.S. 765, 786 (1978).

183. Under traditional first amendment analysis, a state must demonstrate that the regulation effectuates a compelling interest. See *Consolidated Edison Co. v. Public Serv. Comm'n*, 447 U.S.

prohibition on a utility's political speech to be more constitutionally suspect than a similar ban on promotional speech.¹⁸⁵

Under *Central Hudson*, a court is likely to strike down a total ban on informational advertising,¹⁸⁶ even though such a ban is not protected under traditional first amendment principles. The commercial speech cases of *Virginia State Board*¹⁸⁷ and *Bates*,¹⁸⁸ which comprise the underpinnings of the *Central Hudson* test,¹⁸⁹ specifically allowed advertising of informational material.¹⁹⁰ Thus, a state's interest in prohibitory regulation is unlikely to outweigh the value of informational advertising. Even if a regulation could pass the "substantial state interest" part of the test, a total ban on informational advertising would likely fail the "no more extensive than necessary" requirement. Informational advertising benefits consumers.¹⁹¹ Hence, a court would

530, 533-34 (1980); *First Nat'l Bank of Boston v. Bellotti*, 435 U.S. 765, 786 (1978); *Erznoznik v. City of Jacksonville*, 422 U.S. 205, 217 (1975); *Grayned v. City of Rockford*, 408 U.S. 104, 115 (1972); *United States v. O'Brien*, 391 U.S. 367, 376-77 (1968); *NAACP v. Button*, 371 U.S. 415, 438 (1963). Politically oriented advertising by a utility arguably commands more stringent protection because that speech is not prompted primarily by economic reasons. Hence this type of speech is less hardy than speech resting on an economic foundation. See *Virginia State Bd. of Pharmacy v. Virginia Citizens Consumer Council, Inc.*, 425 U.S. 748, 771-72 n.24 (1976).

184. See notes 181-82 *supra* and accompanying text.

185. Under the stricter compelling state interest standard, the Supreme Court has recognized only two narrow exceptions to the first amendment policy of voiding content-based regulations. In *Greer v. Spock*, 424 U.S. 828 (1976), the Court allowed the federal government to prohibit partisan political speech on a United States military base. *Id.* at 840. In *Lehman v. City of Shaker Heights*, 418 U.S. 298 (1974), the Court allowed a city transit system to refuse partisan political advertising in favor of commercial advertising to fill its rental advertising space. The Court thought that the city's fears of jeopardizing long-term commercial revenue and offending paying passengers with potentially offensive political propaganda were justified. *Id.* at 304.

186. See note 83 *supra* and accompanying text.

187. *Virginia State Bd. of Pharmacy v. Virginia Citizens Consumer Council*, 425 U.S. 748 (1976).

188. *Bates v. State Bar*, 433 U.S. 350 (1977).

189. See notes 124-55 *supra* and accompanying text.

190. See *Bates v. State Bar*, 433 U.S. 350, 382 (1977) (advertisements of routine legal services); *Virginia State Bd. of Pharmacy v. Virginia Citizens Consumer Council*, 425 U.S. 748, 765 (1976) (advertisements of drug prices).

191. See *Re Arkansas Power & Light Co.*, 15 PUB. UTIL. REP. (PUR) 4th 153, 176 (Ark. P.S.C. 1976); *Promotional Practices of Elec. Utils.*, 8 PUB. UTIL. REP. (PUR) 4th 268, 276 (Fla. P.S.C. 1975); *Re Idaho Power Co.*, 29 PUB. UTIL. REP. (PUR) 4th 183, 204 (Idaho P.S.C. 1979); *Re Consumers Power Co.*, 14 PUB. UTIL. REP. (PUR) 4th 1, 29 (Mich. P.S.C. 1976). See also Duffy, *supra* note 5, at 8; Netschert, *supra* note 5, at 18.

Although the New York Public Service Commission expressly prohibited promotional advertising, it approved of informational advertising. See *Central Hudson Gas & Elec. Co. v. Public Serv. Comm'n*, 447 U.S. 557, 567 (1980).

probably conclude that a flat ban on informational advertising is unconstitutionally overinclusive, because the prohibition could prevent consumers from receiving valuable information.

A total ban on institutional advertising¹⁹² would similarly fail part four of the *Central Hudson* test as being overly restrictive. The Oklahoma Supreme Court, addressing the constitutionality of a total ban on institutional advertising in a pre-*Central Hudson* case,¹⁹³ specifically concluded that the state could achieve its goal of regulating institutional advertisement by less drastic measures.¹⁹⁴ The Oklahoma court, in effect, based its decision on the same grounds subsequently employed by the United States Supreme Court in the fourth part of the *Central Hudson* test. Furthermore, the Oklahoma court noted that, as in the informational advertising context, consumers benefit, at least to some degree, from institutional advertising.¹⁹⁵ Relying on this determination, a court using the *Central Hudson* analysis would probably hold a total ban on institutional advertising in violation of the least restrictive means requirement. Hence, in the face of a total ban on institu-

192. Institutional advertising may be defined simply as advertising "designed to enhance the public image of the utility." See notes 84-85 *supra* and accompanying text. *State v. Oklahoma Gas & Elec. Co.*, 536 P.2d 887 (Okla. 1975).

193. *State v. Oklahoma Gas & Elec. Co.*, 536 P.2d 887 (Okla. 1975).

194. Commenting on the validity of the direct total ban on institutional advertising, the court concluded: "The same end could be achieved by disallowing such expenditures as operating expenses for ratemaking purposes and this method would not impede the utilities' ability to communicate with the public. *We conclude the prohibition on expenditures for institutional advertising is an unreasonable means of protecting ratepayers from these expenditures.*" *Id.* at 894 (emphasis added). The Missouri Court of Appeals confronted the same issue in a slightly different context in *Laclede Gas Co. v. Public Serv. Comm'n*, 600 S.W.2d 222 (Mo. Ct. App. 1980), *appeal dismissed*, 449 U.S. 1072 (1981). In *Laclede*, the commission refused to allow, as part of operating expenses for ratemaking purposes, \$204,691 of institutional or goodwill advertising. Although the court was not faced with a total ban on institutional advertising, it alluded to the negative consequences of such a prohibition:

The evidence herein does not support Laclede's argument that . . . the P.S.C. violated any constitutional right of Laclede to the exercise of its right of free speech. . . . The order of the P.S.C. does not prohibit advertising by Laclede. If it had, this order would, without question, have violated the constitutional and managerial rights of Laclede.

Id. at 228.

195. 536 P.2d at 895.

Another ratepayer benefit of institutional advertising cited by courts is the attraction of investment capital that reduces the amount of financing needed to operate. The result may be lower rates at the retail level. See *Re Alabama Power Co.*, 97 PUB. UTIL. REP. (PUR) 3d 371, 377 (Ala. P.S.C. 1972); *Re Consolidated Edison Co.*, 73 PUB. UTIL. REP. (PUR) 3d 417, 468 (N.Y.P.S.C. 1968). One commentator suggested that institutional advertising will foster a feeling of goodwill by the consumer toward the utility and will result in the consumer economizing on utility services to achieve the national energy conservation goal. See, Duffy, *supra* note 5, at 6.

tional advertising, a utility may successfully invoke the first amendment commercial speech doctrine.

B. *Cost Allocation Denial*

When a public service commission does not allow a utility to include expenses in operating costs for ratemaking purposes, the utility may seek to defend its cost allocation¹⁹⁶ attempt under the first amendment.¹⁹⁷ In response to this defense, commissions and courts draw a distinction between denying the speech altogether and denying the allocation of advertising costs as part of the ratemaking formula.¹⁹⁸ Utilities, in defending their attempts to allocate costs, usually argue that because the commission refused to charge the advertising to operating costs, the funds for the advertising must come out of shareholder profits.¹⁹⁹ Utilities further assert that a reduction of shareholder profits hinders their ability to attract new investment capital²⁰⁰ and denies shareholders of their regulated, but constitutionally circumscribed, rate of return.²⁰¹ Utilities contend that these financial considerations dis-

196. For purposes of this Note, "cost allocation" is used synonymously with the concept of allowance of advertising cost as part of the ratemaking formula. See notes 9 & 54-81 *supra* and accompanying text.

197. See, e.g., *Laclede Gas Co. v. Public Serv. Comm'n*, 600 S.W.2d 222 (Mo. Ct. App. 1980), *appeal dismissed*, 449 U.S. 1072 (1981); *Rochester Gas & Elec. Corp. v. Public Serv. Comm'n*, 51 N.Y.2d 823, 413 N.E.2d 349, 433 N.Y.S.2d 420 (1980), *appeal dismissed*, 450 U.S. 961 (1981). The Supreme Court in *Central Hudson* reaffirmed the right of utilities to seek cost allocation: "Unregulated businesses pass on promotional costs to consumers, and this Court expressly approved the practice for utilities in West Ohio . . ." 447 U.S. at 568 n.11.

Under the first amendment, if a regulation is void on its face, the speaker may deliver his message in violation of the regulation and defend his actions on the unconstitutionality of the regulation. *Lovell v. City of Griffin*, 303 U.S. 444, 452-53 (1938). Hence, utilities may charge the costs of advertising to operating expenses and subsequently defend their inclusion during test year analysis.

198. See, e.g., *Central Hudson Gas & Elec. Corp. v. New York Pub. Serv. Comm'n*, 447 U.S. 557, 568 n.11 (1980); *Consolidated Edison Co. v. New York Pub. Serv. Comm'n*, 447 U.S. 530, 544 (1980) (Marshall, J., dissenting); *Laclede Gas Co. v. Public Serv. Comm'n*, 600 S.W.2d 222, 228 (Mo. Ct. App. 1980), *appeal dismissed*, 449 U.S. 1072 (1981); *Rochester Gas & Elec. Corp. v. Public Serv. Comm'n*, 51 N.Y.2d 823, 825, 413 N.E.2d 359, 360, 433 N.Y.S.2d 420, 421 (1980), *appeal dismissed*, 450 U.S. 961 (1981).

199. Advertising costs become part of the rate schedule when included in the operating costs of the ratemaking formula: (rate base x rate of return) + operating costs = revenue. Cost included within the revenue amount may be charged to consumers. Those expenses not included must come out of shareholder profits. See notes 54-81 *supra* and accompanying text.

200. See Note, *supra* note 96, at 633 & n.136.

201. See notes 54-64 *supra* and accompanying text.

Some commentators and legislators have argued that ratepayers, in the long run, subsidize those

courage them from engaging in advertising speech.²⁰² When a utility raises a first amendment defense, courts, contrary to past practice,²⁰³ must now evaluate the legitimacy of a cost allocation denial under the *Central Hudson* four-part analysis.²⁰⁴ The likelihood of a successful commercial speech defense under *Central Hudson* depends primarily on the category of advertising and the type of utility-speaker.

1. *Allocation of Informational and Political Advertising: Uniform Treatment of Gas and Electric Utilities*

The validity of allocating informational and political advertising ex-

advertising cost allocations that are denied. They asserted that if shareholders must pay for advertising, dividends will be reduced accordingly. This has a negative effect on potential investors, thereby hindering the utility's ability to attract additional capital for needed growth. Accordingly, utility stock prices become depressed. See THE ENERGY SOURCE BOOK, *supra* note 4, at 92; *Electric Utility Rate Reform and Regulatory Improvement: Hearings on H.R. 12461, H.R. 2633 and H.R. 2650 (Titles VII and VIII), H.R. 6696, H.R. 10869, H.R. 11449, H.R. 11475, H.R. 12848, H.R. 12872 Before the Subcomm. on Energy Power of the House Comm. on Interstate and Foreign Commerce*, 94th Cong., 2d Sess., pt. 1, 227 (1976). *Accord*, Brief for Appellants at 47, *Laclede Gas Co. v. Public Serv. Comm'n*, 600 S.W.2d 222 (Mo. Ct. App. 1980), *appeal dismissed*, 449 U.S. 1072 (1981). To compensate for the lack of investment, utilities must borrow needed capital at inflated interest rates. See A. FINDER, *supra* note 6, at 8. Inflated capital costs force utilities to increase rates. See *National Energy Act Hearings*, *supra* note 99, pt. 3, vol. 1, at 68-75. As a result, consumers pay for the advertising in the end. See Note, *supra* note 96, at 633 & n.136.

202. See, e.g., *Laclede Gas Co. v. Public Serv. Comm'n*, 600 S.W.2d 222, 226 (Mo. Ct. App. 1980), *appeal dismissed*, 449 U.S. 1072 (1981); *Rochester Gas & Elec. Corp. v. Public Serv. Comm'n*, 51 N.Y.2d 823, 824, 413 N.E.2d 359, 360, 433 N.Y.S.2d 420, 421 (1980), *appeal dismissed*, 450 U.S. 961 (1981).

Alternatively, if the costs of advertising cannot be passed on to the consumer, the economic incentive that places the advertising in the commercial speech realm is absent. Accordingly, the advertising is no longer commercial speech because it would be unprofitable for the utility to continue to engage in it. The speech should then be entitled to the more protective evaluation standard for traditional or pure speech. See *generally* note 132 *supra*.

203. Prior to the adoption of the *Central Hudson* test, courts evaluated the validity of advertising expense allocation on various grounds, including conservation, see, e.g., *Re Gas Co.*, 35 PUB. UTIL. REP. (PUR) 4th 106 (N.M.P.S.C. 1980); no benefit to ratepayers, see, e.g., *Re Minnesota Gas Co.*, 32 PUB. UTIL. REP. (PUR) 4th 1 (S.D.P.U.C. 1979); environmental concerns, see, e.g., *In re Hawaiian Elec. Co.*, 56 Hawaii 260, 535 P.2d 1102 (1975); economic concerns, see, e.g., *Promotional Practices of Elec. Utils.*, 8 PUB. UTIL. REP. (PUR) 4th 268 (Fla. P.S.C. 1975). This practice continues unabated today. See notes 107-09 *supra* and accompanying text.

At least one regulatory commission requires a utility to include with the advertisement a "tag" stating that the advertisement is paid out of shareholder funds and not with those of consumers. See *Re Rule Making Relating to Advertising Expenditures*, 39 PUB. UTIL. REP. (PUR) 4th 295 (N.C. Utils. Comm'n 1980). But see *Re Advertising Practices of Tel., Elec. & Gas Distribution Cos.*, 35 PUB. UTIL. REP. (PUR) 4th 361 (N.J. Bd. Pub. Utils. 1980).

204. See notes 151-55 *supra* and accompanying text. Although the Supreme Court considered a total prohibition in *Central Hudson*, Justice Powell, writing for the majority, briefly addressed the cost allocation issue. See 447 U.S. at 568 n.11.

penses to operating costs does not hinge on the nature of the utility-speaker. It depends, rather, on the four *Central Hudson* criteria: whether the advertising is misleading or related to the unlawful; whether the denial of allocation promotes a substantial state interest; whether the state interest is effectuated by direct regulatory means; and whether that regulation is no more extensive than necessary.²⁰⁵

Courts should uphold allocation of informational²⁰⁶ advertising expenses under a *Central Hudson* analysis. Both shareholders and rate-payers benefit from informational advertising.²⁰⁷ Public service commissions and consumer groups traditionally have proffered several state interests when denying allocation of advertising expenditures, including conservationist,²⁰⁸ environmental,²⁰⁹ and economic²¹⁰ con-

205. See notes 151-55 *supra* and accompanying text.

206. See note 83 *supra* for a definition of informational advertising.

207. See, e.g., *Re Arkansas Power & Light Co.*, 15 PUB. UTIL. REP. (PUR) 4th 153 (Ark. P.S.C. 1976); *Re Idaho Power Co.*, 29 PUB. UTIL. REP. (PUR) 4th 183 (Idaho P.U.C. 1979); *Re Commonwealth Edison Co.*, 35 PUB. UTIL. REP. (PUR) 4th 49 (Ill. Commerce Comm'n 1980); *Re Interstate Power Co.*, 32 PUB. UTIL. REP. (PUR) 4th 494 (Minn. P.S.C. 1979); *Re Advertising Practices of Tel., Elec., & Gas Distribution Cos.*, 35 PUB. UTIL. REP. (PUR) 4th 361 (N.J. Bd. Pub. Utils. 1980); *Re South Carolina Elec. & Gas Co.*, 34 PUB. UTIL. REP. (PUR) 4th 458 (S.C.P.S.C. 1980). Informational advertising promotes efficient use of resources because it provides consumers with data as to which competitive fuel is the better alternative. See Brief for Appellants at 22, *Laclede Gas Co. v. Public Serv. Comm'n*, 600 S.W.2d 222 (Mo. Ct. App. 1980), *appeal dismissed*, 449 U.S. 1072 (1981) (testimony of witness before Missouri Public Service Commission rate hearing); Note, *supra* note 10, at 107 n.118 (allowance of advertising against interfuel competitors aids the public in making an informed choice between available alternatives).

208. See, e.g., *Central Hudson Gas & Elec. Co. v. Public Serv. Comm'n*, 447 U.S. 557 (1980); *Re Commonwealth Edison Co.*, 35 PUB. UTIL. REP. (PUR) 4th 49 (Ill. Commerce Comm'n 1980); *Re Michigan Power Co.*, 18 PUB. UTIL. REP. (PUR) 4th 418 (Mich. P.S.C. 1977); *Re Advertising Practices of Tel., Elec., & Gas Distribution Cos.*, 35 PUB. UTIL. REP. (PUR) 4th 361 (N.J. Bd. Pub. Utils. 1980); *Re Gas Co.*, 35 PUB. UTIL. REP. (PUR) 4th 106 (N.M.P.S.C. 1980); *Re South Carolina Elec. & Gas Co.*, 34 PUB. UTIL. REP. (PUR) 4th 458 (S.C.P.S.C. 1980); *Rochester Gas & Elec. Corp.*, 14 PUB. UTIL. REP. (PUR) 4th 475 (N.Y.P.S.C. 1976).

209. See, e.g., *In re Hawaiian Elec. Co.*, 56 Hawaii 260, 535 P.2d 1102 (1975); *Re Public Serv. Co.*, 13 PUB. UTIL. REP. (PUR) 4th 40 (Colo. P.U.C. 1975); *Re Promotional Practices of Elec. Utils.*, 8 PUB. UTIL. REP. (PUR) 4th 268 (Fla. P.S.C. 1975). See also National Environmental Policy Act of 1969, 42 U.S.C. § 4321 (1976).

210. See, e.g., *Re Promotional Practices of Elec. Utils.*, 8 PUB. UTIL. REP. (PUR) 4th 268 (Fla. P.S.C. 1975); *Re Detroit Edison Co.*, 3 PUB. UTIL. REP. (PUR) 4th 209 (Mich. P.S.C. 1974); *Re Gas Co.*, 35 PUB. UTIL. REP. (PUR) 4th 106 (N.M.P.S.C. 1980); *Re Minnesota Gas Co.*, 32 PUB. UTIL. REP. (PUR) 4th 1 (S.D.P.S.C. 1979). Economic concerns involve inflation, benefit to the consumer, and cost control. See note 109 *supra*.

The demise of the efficiencies of economies of scale began in the late 1960s. The spiraling costs of new plant construction and generating plant fuel now outstrip the efficiencies of large generating capacity economies of scale. See note 99 *supra*. In effect, it is no longer economically prudent for electric utilities to encourage consumption. See *id.*

cerns. These recognized or purported state interests, however, neither conflict with nor outweigh the value of informational advertising. Although conservationist, environmental, and economic concerns may be legitimate state interests,²¹¹ they are not directly promoted by disallowing informational advertising costs. Furthermore, informational advertising that includes energy conserving time-of-day rate ads,²¹² consumer oriented customer service ads,²¹³ and information-disseminating public service ads²¹⁴ does not infringe on these asserted state interests. Accordingly, a refusal to allocate informational advertising expenses fails the direct means²¹⁵ requirement of *Central Hudson*. Yet, even if some expenses for informational advertising are not warranted,

211. Courts must consider the issue of whether the preservation of managerial prerogative is a substantial state interest. Managerial prerogative involves [the] responsibility of the duly authorized manager of a utility to decide the type, quantity or form of advertising which would most benefit the corporation in its continued growth. . . . The function of [a public service commission] . . . is that of regulation, and not of management. . . . [It] should not be allowed to interfere with the proper operation of the utility as a business concern by usurping managerial prerogatives. *Alabama Power Co. v. Alabama Pub. Serv. Comm'n*, 359 So. 2d 776, 780 (Ala. 1978). *Accord*, *West Ohio Gas Co. v. Ohio Pub. Utils. Comm'n*, 294 U.S. 63, 72 (1935) (“[i]n the absence of a showing of inefficiency or improvidence, a court will not substitute its judgment for theirs as to the measure of a prudent outlay”). Under the managerial prerogative analysis, advertising expenditures are evaluated on a “reasonableness” standard as to amount. *See, e.g., Central Me. Power Co. v. Maine Pub. Utils. Comm'n*, 153 Me. 228, 244, 136 A.2d 726, 736-37 (1957); *New England Tel. & Tel. Co. v. Department of Pub. Utils.*, 360 Mass. 443, 493-94, 275 N.E.2d 493, 524 (1971); *State ex rel. Dyer v. Public Serv. Comm'n*, 341 S.W.2d 795, 802 (Mo. 1960). The recent trend, however, has been to give the “reasonableness” standard a different meaning. *See* notes 100-09 *supra* and accompanying text.

Contemporary courts and public service commissions analyze advertising expenditures on the basis of benefit to the consumer, *see, e.g., Re Minnesota Gas Co.*, 32 PUB. UTIL. REP. (PUR) 4th 1, 23-26 (S.D.P.U.C. 1979) (institutional and promotional advertising disallowed as part of operating expense because not of benefit to consumers), and content-based social policies, *see, e.g., Re Commonwealth Edison Co.*, 35 PUB. UTIL. REP. (PUR) 4th 49, 67 (Ill. Commerce Comm'n 1980) (allowing advertising expenses related only to conservation, energy efficiency, and safety). *See generally* Note, *supra* note 10, at 95-96. *See also In re Hawaiian Elec. Co.*, 56 Hawaii 260, 535 P.2d 1102 (1975) (environmental concerns).

To resolve this tension between upholding the managerial prerogative concept and promoting content-based social policies, courts must balance the two interests and decide under a *Central Hudson* analysis which is more substantial.

212. *See, e.g.,* Notice of Proposal, *supra* note 5, at 2-R, 3-R.

213. *See, e.g., Re Peoples Gas Light & Coke Co.*, 34 PUB. UTIL. REP. (PUR) 4th 292 (Ill. Commerce Comm'n 1979); *Re Determination of Whether Advertising Rules Conform to Pub. Util. Regulatory Policies Act of 1978*, No. 35723 (Ind. P.S.C. 1980).

214. *See, e.g., Re Advertising Practices of Tel., Elec., & Gas Distribution Cos.*, 35 PUB. UTIL. REP. (PUR) 4th 361 (N.J. Bd. Pub. Utils. 1980).

215. *See* note 153 *supra* and accompanying text.

a court must make a partial allocation²¹⁶ to satisfy the "least restrictive means"²¹⁷ requirement. A complete disallowance of any expenditures legitimately chargeable to ratepayers would violate this standard. Hence, a commission should remove from the rate schedule only those expenditures that clearly conflict with the state's substantial interest. In addition, if the advertisement purporting to convey an informational message is deceptive or related to unlawful activity,²¹⁸ cost allocation is disallowed under the *Central Hudson* test.

Allocation of political advertising expenses is more difficult to justify than informational advertising expenses. Even though *Bellotti*²¹⁹ and *Consolidated Edison*²²⁰ may signify the need to evaluate politically oriented advertising on the more protective, traditional first amendment grounds,²²¹ the denial of allocation of expenses does not, of itself, prohibit that speech altogether. A utility still may engage in political speech; it simply may not force ratepayers to subsidize that speech. Neither *Bellotti* nor *Consolidated Edison* can be read to stand for any broader proposition.²²²

Whether a hybrid type of political advertising, such as politically charged promotional advertising,²²³ is allowed as an operating cost will depend on the substantial state interest involved. Under the *Central Hudson* approach, a court must balance the speech and regulation interests.²²⁴ When running pronuclear power advertisements, for example, a utility may have a distinct interest in speaking on important

216. Partial cost allocation of advertising expenses may present problems of computation accuracy. See, e.g., *Re Brooklyn Union Gas Co.*, 39 PUB. UTIL. REP. (PUR) 4th 388, 397, (N.Y.P.S.C. 1980) (noting difficulty in assessing accurately the extent to which consumer rates benefitted from promotional advertising). Several states, however, have surmounted the logistical problems of partial allocations. See *Re Peoples Gas Light & Coke Co.*, 35 PUB. UTIL. REP. (PUR) 4th 292, 317 (Ill. Commerce Comm'n 1979); *Re Columbia Gas*, 70 Md. P.S.C. 187 (1979) (Order No. 63812).

217. See note 154 *supra* and accompanying text.

218. See note 151 *supra* and accompanying text.

219. *First Nat'l Bank of Boston v. Bellotti*, 435 U.S. 765 (1978).

220. *Consolidated Edison Co. v. Public Serv. Comm'n*, 447 U.S. 530 (1980).

221. See notes 169-85 *supra* and accompanying text.

222. The Supreme Court specifically avoided the cost allocation issue for political advertising in *Consolidated Edison*. See 447 U.S. at 543 n.13; *id.* at 544 (Marshall, J., concurring).

223. See PUB. UTIL. FORT., Nov. 8, 1979 at 51, 54 (nuclear power advertising as an example of promotional advertising with political overtones). See, e.g., *Re Public Serv. Co.*, F.C. No. 2548 (N.H.P.S.C. July 31, 1980) (expense of Seabrook Station Education Center explaining nuclear generation concepts disallowed as institutional advertising designed to promote the image of the utility).

224. See note 147 *supra* and accompanying text.

industry-related matters.²²⁵ Furthermore, utilities have evidence²²⁶ demonstrating that nuclear technology facilitates economical production of electricity and ultimately decreases retail costs.²²⁷ The state, on the other hand, has a substantial interest in not having ratepayers subsidize activities for which they receive no benefit and to which they are philosophically opposed.²²⁸ Furthermore, some state commissions argue that allowance of these costs as part of the rate schedule would violate the ratepayers' first amendment rights.²²⁹

In deciding whether to allow an allocation of political advertising costs, a court must balance countervailing interests. To the extent that political advertising benefits ratepayers and outweighs any other state interest in refusing allocation, the commission should allow the utility to charge this advertising cost to the rate schedule. Moreover, when allocation is justified, a commission should allocate the appropriate parts of the advertising expenses so as to satisfy the least restrictive means requirement of *Central Hudson*.²³⁰ On the other hand, the commission should not charge to the retail rate²³¹ those costs that do not

225. See *Re Central Me. Power Co.*, 15 PUB. UTIL. REP. (PUR) 4th 455 (Me. P.U.C. 1976); *Re Rochester Gas & Elec. Corp.*, 14 PUB. UTIL. REP. (PUR) 4th 475 (N.Y.P.S.C. 1976); *Re Narragansett Elec. Co.*, 23 PUB. UTIL. REP. (PUR) 4th 516 (R.I.P.S.C. 1978).

226. See, e.g., *Re Wisconsin Elec. Power Co.*, 9 PUB. UTIL. REP. (PUR) 4th 204 (Wis. P.S.C. 1975).

227. See THE ENERGY SOURCE BOOK, *supra* note 4, at 92-93. See generally Huntington, *The Rapid Emergence of Marginal Cost Pricing in the Regulation of Utility Rate Structures*, 55 B.U.L. REV. 689 (1975).

228. See *Re Portland Gen. Elec. Co.*, 8 PUB. UTIL. REP. (PUR) 4th 393 (Or. P.U.C. 1974). Justice Blackmun, in dissent in *Consolidated Edison*, voiced concern over this issue: "I do not accept appellant's argument that preventing a 'free ride' for the utility's message, is not a substantial, legitimate state concern. Even though the free ride may cost the ratepayers nothing additional by way of specific dollars, it still qualifies as forced support of the utility's speech." 447 U.S. at 552 (Blackmun, J., dissenting). *Accord*, Note, *Utility Companies and the First Amendment: Regulating the Use of Political Inserts in Utility Bills*, 64 VA. L. REV. 921, 926 (1978).

229. See *Consolidated Edison Co. v. Public Serv. Comm'n*, 447 U.S. 530 (1980); *id.* at 548 (Blackmun, J., dissenting); *Rochester Gas & Elec. Corp. v. Public Serv. Comm'n*, 51 N.Y.2d 823, 413 N.E.2d 349, 433 N.Y.S.2d 420 (1980), *appeal dismissed*, 450 U.S. 961 (1981). Each cited *Abood v. Detroit Bd. of Educ.*, 431 U.S. 209 (1977). The courts in *Consolidated Edison* and *Rochester* avoided deciding the issue. Justice Powell in *Consolidated Edison* repelled the notion by stating: "Because the Commission has failed to demonstrate that such costs could not be allocated between shareholders and ratepayers, we have no occasion to decide whether the rule of *Abood* . . . would prevent Consolidated Edison from passing on . . . the costs . . ." 447 U.S. at 543-44 n.13.

230. See note 216 *supra* and accompanying text.

231. See *Re The Narragansett Elec. Co.*, 23 PUB. UTIL. REP. (PUR) 4th 515 (R.I.P.S.C. 1978) (court disallowed the portion of pro-nuclear power advertising found not of benefit to consumers). See also *Boushey v. Pacific Gas & Elec. Co.*, 10 PUB. UTIL. REP. (PUR) 4th 23 (Cal. P.U.C. 1975);

benefit consumers, even in the face of a utility claim that denial infringes its speech.²³² If the utility believes the advertising message is important enough, it will likely advertise at shareholder expense.²³³

2. *Allocation of Institutional and Promotional Advertising: Effect of Interfuel Competition*

In some geographic areas, gas and electric utilities directly compete with one another for the same consumer market. This interfuel competition²³⁴ requires separate consideration for each utility in discussing the allocation of institutional and promotional advertising expenditures.

a. Electric Utilities: Institutional and Promotional Advertising

Until recently, regulatory commissions allowed electric utilities to al-

In re Investigation into the Advertising and Promotional Practices of Regulated Iowa Pub. Utils., No. U-463 (Iowa State Commerce Comm'n Jan. 29, 1975); *Re* Cascade Natural Gas Corp., 8 PUB. UTIL. REP. (PUR) 4th 19 (Or. P.U.C. 1974).

232. See *Laclede Gas Co. v. Public Serv. Comm'n*, 600 S.W.2d 222, 226 (Mo. Ct. App. 1980), *appeal dismissed*, 449 U.S. 1072 (1981); *Rochester Gas & Elec. Corp. v. Public Serv. Comm'n*, 64 A.D.2d 345, 410 N.Y.S.2d 142 (1978), *aff'd*, 51 N.Y.2d 823, 413 N.E.2d 359, 433 N.Y.S.2d 470 (1980), *appeal dismissed*, 450 U.S. 961 (1981). Justice Powell recognized this argument in *Central Hudson*: "There may be a greater incentive for a utility to advertise if it can use promotional expenses in determining its rate of return, rather than pass those costs on solely to shareholders." 447 U.S. at 557, 568 n.11.

233. See Pierson, *Sales-Related and Institutional Advertising: The Case of Rate-Regulated Public Utilities*, in *THE POLITICAL ECONOMY OF ADVERTISING* 187, 207 (D. Tuerck ed. 1978). This concept is echoed in Justice Blackmun's dissent in *Consolidated Edison*: "Due to the greater likelihood that a recipient would read an insert with the bill, the utility well might desire to place its insert with the bill even if the total cost of the mailing were charged to the shareholders." 447 U.S. at 554 n.4 (1980) (Blackmun, J., dissenting) (citations omitted). See also Note, *supra* note 96, at 604 n.9.

234. Interfuel competition for purposes of this Note is defined as competition between utilities selling a different fuel product in the same market area. See *West Ohio Gas Co. v. Public Utils. Comm'n*, 294 U.S. 63, 72 (1935). In *West Ohio Gas*, Justice Cardozo stated:

The suggestion is made that there is no evidence of competition. We take judicial notice of the fact that *gas is in competition with other forms of fuel*, such as oil and electricity. A business never stands still. It either grows or decays. Within the limits of reason, advertising or development expenses to foster normal growth are legitimate charges upon income for rate purposes as for others.

Id. (emphasis added).

Those utilities that provide both gas and electric service are grouped with the all-electric utilities for the purposes of this Note. Studies show that combined gas-electric utilities advertise less than utilities that must engage in interfuel competition. See Wilder, *Public Utility Advertising: Some Observations*, 49 LAND. ECON. 458-62 (1973).

locate institutional advertising to the rate schedule.²³⁵ This policy reflected the economic belief, widely espoused prior to the 1970s, that utilities should maximize their resources to benefit from great economies of scale.²³⁶ As economic and philosophical conditions changed,²³⁷ regulatory commissions began the current trend of disallowing institutional advertising cost allocation. This change is due partly to the belief that the benefits from this advertising inure only to shareholders.²³⁸ Moreover, some courts consider institutional advertising a questionable endeavor altogether.²³⁹

Institutional advertising is designed to enhance the utility's public image.²⁴⁰ If the advertisement projects a misleading or false image of the electric utility, cost allocation will be denied under the *Central Hudson* test, which denies first amendment protection for speech "misleading or relating to the unlawful."²⁴¹ As with a direct prohibition on institutional advertising,²⁴² *Central Hudson* probably would prevent a

235. See, e.g., *Re Alabama Power Co.*, 97 PUB. UTIL. REP. (PUR) 3d 371 (Ala. P.S.C. 1972); *Re Central Me. Power Co.*, 8 PUB. UTIL. REP. (PUR) 4th 277 (Me. P.U.C. 1975); *Re Union Elec. Co.*, 29 PUB. UTIL. REP. (PUR) 3d 254 (Mo. P.S.C. 1959); *State v. Oklahoma Gas & Elec. Co.*, 536 P.2d 887 (Okla. 1975); *Re Wisconsin Elec. Power Co.*, 9 PUB. UTIL. REP. (PUR) 4th 204 (Wis. P.S.C. 1975).

236. See notes 23-27 & 91-98 *supra* and accompanying text.

237. See notes 99-102 *supra* and accompanying text.

238. See, e.g., *Re Arkansas Power & Light Co.*, 15 PUB. UTIL. REP. (PUR) 4th 153 (Ark. P.S.C. 1976); *Re Public Serv. Co.*, 13 PUB. UTIL. REP. (PUR) 4th 40 (Colo. P.U.C. 1975); *Re Commonwealth Edison Co.*, 35 PUB. UTIL. REP. (PUR) 4th 49 (Ill. Commerce Comm'n 1980); *Re Potomac Elec. Power Co.*, 10 PUB. UTIL. REP. (PUR) 4th 13 (Md. P.S.C. 1975); *Re Interstate Power Co.*, 32 PUB. UTIL. REP. (PUR) 4th 494 (Minn. P.S.C. 1979); *Re Minn. Gas Co.*, 32 PUB. UTIL. REP. (PUR) 4th 1 (S.D.P.S.C. 1979); *Re Madison Gas & Elec. Co.*, 34 PUB. UTIL. REP. (PUR) 4th 569 (Wis. P.S.C. 1980).

239. The New York Supreme Court, Appellate Division, in discussing what it designated "information" advertising (but what in effect was institutional advertising) stated:

Assuming for present purposes that a corporate body or person has the full and complete protection of the constitutional right to freedom of speech unrelated to the immediate cultivation of profit and income in the matter of public service, or freedom of educating the public, as propaganda is often entitled, the present record discloses no interference with that right . . . [I]t is certain that the consumers are not concerned with such niceties as the image of a utility.

Rochester Gas & Elec. Corp. v. Public Serv. Comm'n, 64 A.D.2d 345, 351, 410 N.Y.S.2d 142, 146 (1978) (emphasis added), *aff'd*, 51 N.Y.2d 823, 413 N.E.2d 359, 433 N.Y.S.2d 420 (1980), *appeal dismissed*, 450 U.S. 961 (1981). See *Re Commonwealth Edison Co.*, 35 PUB. UTIL. REP. (PUR) 4th 49 (Ill. Commerce Comm'n 1980); *Re Madison Gas & Elec. Co.*, 34 PUB. UTIL. REP. (PUR) 4th 589 (Wis. P.S.C. 1980).

240. See notes 84-85 *supra* and accompanying text.

241. See note 151 *supra* and accompanying text.

242. See notes 14-17 *supra* and accompanying text.

commission from disallowing the allocation of all or part of such an advertising cost. Under part two of the test, the asserted substantial state interest is having the consumers pay for only that which benefits them.²⁴³ The court must balance this interest against the electric utility's argument that image building advertising facilitates the attraction of new capital needed to sustain service levels and meet expansion needs.²⁴⁴ This argument, however, was unsuccessful in at least two states and is not likely to prevail over the state's "benefit to the consumer" interest.²⁴⁵ Moreover, the speculative nature of public relations programs makes the specific amount of consumer benefit from institutional advertising difficult to measure accurately. Faced with this uncertainty, some courts may be inclined to disallow completely allocation of these costs. Those courts should be mindful, however, of the least restrictive means requirement of *Central Hudson*.²⁴⁶ To comply with this requirement, a court must fashion a partial allocation of the electric utility advertising expenses to the extent that consumers receive a benefit.²⁴⁷

Cost allocation of electric utility promotional advertising, also once allowed and even encouraged,²⁴⁸ is now regularly denied. Regulatory commissions justify this current trend by citing energy,²⁴⁹ environmen-

243. See cases cited note 238 *supra*.

244. See *Re Alabama Power Co.*, 97 PUB. UTIL. REP. (PUR) 3d 371 (Ala. P.S.C. 1972); *Re Consolidated Edison Co.*, 73 PUB. UTIL. REP. (PUR) 3d 417 (N.Y.P.S.C. 1968); *Re Consolidated Edison Co.*, 41 PUB. UTIL. REP. (PUR) 3d 305 (N.Y.P.S.C. 1961). In the 1961 *Consolidated Edison* ruling, institutional advertisement was credited with producing benefit to both consumers and shareholders: "To the extent that such advertising fosters sound consumer relations or encourages people to invest in the company, it seems clear that the consumers, as well as the stockholders, are ultimately benefitted through the lessening of the expense of doing business." *Consolidated Edison Co.*, 41 PUB. UTIL. REP. (PUR) 3d 305, 364 (N.Y.P.S.C. 1961).

At least one commentator suggested that public relations advertising may foster goodwill between customer and utility, thus resulting in an "economizing" of utility services. See Duffy, *supra* note 5, at 9.

245. See *Re General Tel. Co.*, 19 PUB. UTIL. REP. (PUR) 4th 227 (Fla. P.S.C. 1977); *Cornhusker State Tel. Co.*, 13 PUB. UTIL. REP. (PUR) 4th 314 (Neb. P.S.C. 1976). Although both decisions involve telephone utilities, they are useful by analogy to gas and electric utility decisions.

246. See note 154 *supra* and accompanying text.

247. See note 216-17 *supra* and accompanying text.

248. See, e.g., *West Ohio Gas Co. v. Ohio Pub. Utils. Comm'n*, 294 U.S. 63 (1935); *City of El Dorado v. Arkansas Pub. Serv. Comm'n*, 235 Ark. 812, 362 S.W.2d 680 (1962); *Central Me. Power Co. v. Maine Pub. Utils. Comm'n*, 153 Me. 228, 136 A.2d 726 (1957); *State ex rel. Dyer v. Missouri Pub. Serv. Comm'n*, 341 S.W.2d 795 (Mo. 1960).

The incidence of increased consumption was solicited in order to benefit from the economies of scale, thereby reducing costs. See *State v. Oklahoma Gas & Elec. Co.*, 536 P.2d 887 (Okla. 1975).

249. See, e.g., *Re Promotional Practices of Elec. Utils.*, 8 PUB. UTIL. REP. (PUR) 4th 268 (Fla.

tal,²⁵⁰ and economic concerns.²⁵¹ Under a *Central Hudson* analysis, these interests must be weighed against the electric utility's arguments that promotional advertising costs should be passed on to the consumer.²⁵²

Electric utility management justifies promotional advertising cost allocation by arguing that a refusal to allocate costs will result in a reduction of shareholder profits.²⁵³ This result acts as a disincentive to advertise.²⁵⁴ Accordingly, utilities assert that they are hesitant to engage in promotional advertising for fear of undesirable financial ramifications. Another management justification is that promotion of electric heating may convince users of home heating oil to switch to electricity, thereby encouraging conservation of scarce petroleum resources.²⁵⁵

b. Gas Utilities: The Impact of Interfuel Competition on Institutional and Promotional Advertising Cost Allocation

The *Central Hudson* limitation on cost allocation of electric utility advertising does not apply automatically to a gas utility's attempt to allocate promotional advertising costs. Gas utilities often engage in interfuel competition with electric utilities.²⁵⁶ In those markets, gas utili-

P.S.C. 1975); *In re Hawaiian Elec. Co.*, 56 Hawaii 260, 535 P.2d 1102 (1975); *Re Michigan Power Co.*, 18 PUB. UTIL. REP. (PUR) 4th 418 (Mich. P.S.C. 1977); cases cited in notes 107 & 208 *supra*.

250. See *Pacific Gas & Elec. Co.*, 87 PUB. UTIL. REP. (PUR) 3d 270 (Cal. P.U.C. 1971); *Re Public Serv. Co.*, 13 PUB. UTIL. REP. (PUR) 4th 40 (Colo. P.U.C. 1975); *In re Hawaiian Elec. Co.*, 56 Hawaii 260, 535 P.2d 1102 (1975); cases cited in notes 108 & 209 *supra*.

251. *Re Gas Co.*, 35 PUB. UTIL. REP. (PUR) 4th 106 (N.M.P.S.C. 1980); *Re Minnesota Gas Co.*, 32 PUB. UTIL. REP. (PUR) 4th 1 (S.D.P.S.C. 1979); cases cited in notes 109 & 210 *supra*.

252. See note 199 *supra* and accompanying text.

253. See note 200 *supra* and accompanying text.

254. See note 202 *supra* and accompanying text.

255. See Heller, *Restrictions on Electric Utility Advertising Must Go!*, PUB. UTIL. FORT., Dec. 19, 1980, at 29, 30.

Approximately 21.3% of the homes in the United States used fuel oil or kerosene as a primary source of heat. See THE ENERGY FACTBOOK, *supra* note 4, at 36. Consumers have shown a propensity to switch from gas and oil to electricity. See THE ENERGY SOURCE BOOK, *supra* note 4, at 96. In 1977, 50.6% of all new homes completed in that year were heated by electricity. See THE ENERGY FACTBOOK, *supra* note 4, at 38.

If the *Central Hudson* substantial state interest test is now the proper standard by which to evaluate gas and electric utility advertising, promotional advertising designed to convince users of home heating oil to switch to electricity would serve energy conservation, a recognized substantial state interest. In this context, cost allocation could not be denied under the substantial state interest part of *Central Hudson*.

256. Electricity tends to displace the use of gas and oil as the primary heating system in the residential sector. See THE ENERGY SOURCE BOOK, *supra* note 4, at 96. This trend is most evident in the newly completed home market. In 1976 and 1977 approximately 50% of all newly

ties are placed at a distinct disadvantage because virtually every home in any given competitive market area will need electricity for lighting and most appliances.²⁵⁷ Gas, by contrast, is used only for some appliances and home heating and is less indigenous to domestic use.²⁵⁸ This inherent disadvantage compels gas utilities, in order to remain competitive, to solicit customers by advertising more zealously than electric utilities.²⁵⁹ This added measure of advertising is merely an integral part of a gas utility's ordinary operating expenses.²⁶⁰ Accordingly, promotional advertising cost allocation is recognized in many jurisdictions as essential to gas utility viability.²⁶¹

Courts must take notice of the unequal position of gas and electric utilities. Under *Central Hudson* a court must weigh the asserted state interest against the utility's interest in promotional advertising cost al-

constructed homes were heated by electricity. See THE ENERGY FACTBOOK, *supra* note 4, at 38. During this same period, the percentage of newly completed homes heating with gas consistently declined to below 39%. See *id.*

257. In 1979, 99.8% of all homes in the United States were wired for electrical appliances. See THE ENERGY FACTBOOK, *supra* note 4, at 47. Electricity is used to power most household appliances, including air conditioners, dishwashers, clothes dryers, ranges, freezers, refrigerators, televisions, washers, and lighting. See *id.*

258. Only 55% of all housing units utilized gas for heating in 1977. See *id.* at 36. The uses of gas to operate appliances is less extensive and more specialized. In addition to home space and water heating, gas is used for air conditioning, gas grills, gas lights, and clothes dryers. See *id.* at 462.

259. Promotional advertising enables a gas utility to compete with an interfuel competitor. The degree of competition determines and justifies the reasonableness of advertising costs. See Duffy, *supra* note 5, at 9.

The gas utility industry is recognized by the Missouri Public Service Commission as a "high risk" business in which a utility "may lose (because of the gas supply shortage generally endemic in the industry) customer after customer to alternate fuels and eventually lose all its customers." Brief for Appellant at 50-51, *Laclede Gas Co. v. Public Serv. Comm'n*, 600 S.W.2d 222 (Mo. Ct. App. 1980) (citing findings of Missouri Public Service Commission), *appeal dismissed*, 449 U.S. 1072 (1981). For data on projected supplies of natural gas, see note 263 *infra*.

260. *Re Advertising Practices of Tel., Elec., & Gas Distribution Cos.*, 35 PUB. UTIL. REP. (PUR) 4th 361 (N.J. Bd. Pub. Utils. 1980); *Re National Fuel Gas Distribution Corp.*, No. 80-10 (N.Y.P.S.C. Mar. 13, 1980).

261. See, e.g., *West Ohio Gas Co. v. Ohio Pub. Utils. Comm'n*, 294 U.S. 63 (1935); *Re Arkansas La. Gas Co.*, 40 PUB. UTIL. REP. (PUR) 3d 209 (Ark. P.S.C. 1961); *Pacific Gas & Elec. Co.*, 87 PUB. UTIL. REP. (PUR) 3d 270 (Cal. P.U.C. 1971); *Re Southern Cal. Gas Co.*, 35 PUB. UTIL. REP. (PUR) 3d 300 (Cal. P.U.C. 1960); *Re San Diego Gas & Elec. Co.*, 26 PUB. UTIL. REP. (PUR) 3d 129 (Cal. P.U.C. 1958); *Re Union Elec. Co.*, 81 PUB. UTIL. REP. (PUR) 3d 85 (Ill. Commerce Comm'n 1969); *State ex rel. Util. Comm'n v. Piedmont Natural Gas Co.*, 254 N.C. 536, 119 S.E.2d 469 (1961); *Montana-Dakota Utils. Co.*, 22 PUB. UTIL. REP. (PUR) 3d 505 (N.D.P.U.C. 1958); *City of Milwaukee v. Milwaukee Gas Light Co.*, 92 PUB. UTIL. REP. (PUR) (New Series) 133 (Wis. P.S.C. 1952).

location.²⁶² A gas utility's unique need for promotional advertising should outweigh any asserted state conservation interest.²⁶³

Moreover, gas utility promotional advertising serves substantial state environmental and economic interests. Natural gas is the cleanest burning of the fossil fuel energy group.²⁶⁴ By promoting the use of gas, a utility furthers the state's interest in environmental protection. The promotion of gas consumption also supports a state concern for prudent economic policy. First, the principle of economies of scale is still largely operative in the gas utility industry.²⁶⁵ Additionally, promotional advertising by gas utilities encourages the most economic use of available resources. Heating with electricity instead of gas is more expensive and less efficient.²⁶⁶ Relative to electricity, consumption of gas

262. See note 153 *supra* and accompanying text.

263. From 1969 to 1975, gas was in a relative state of short supply. See R. PIERCE, G. ALLISON & P. MARTIN, *supra* note 4, at 448. When supply is low, a state can rightfully assert a substantial interest in preventing promotion of consumption of a scarce fuel. Conversely, if supply is sufficient to meet expanded need, promotional advertising cost allocation should be allowed because the increased consumption would further the benefits of economies of scale. See, e.g., *Re Brooklyn Union Gas Co.*, 27 PUB. UTIL. REP. (PUR) 4th 452 (N.Y.P.S.C. 1978). Recent studies and projections indicate that natural gas supplies will be abundant for the foreseeable future. See PUB. UTIL. FORT., Sept. 10, 1981, at 46; *id.*, at 13; *id.*, June 15, 1981, at 37; *id.*, Feb. 12, 1981, at 41.

264. See THE ENERGY SOURCE BOOK, *supra* note 4, at 283; R. PIERCE, G. ALLISON & P. MARTIN, *supra* note 4, at 457. The fossil fuel energy group includes the following primary fuel sources: coal, natural gas, and petroleum. See THE ENERGY FACT BOOK, *supra* note 4, at 10. These three fuels provide the bulk of total energy consumed by the end-use sector. For example, in 1979, 78.787 quadrillion Btu of energy were consumed in the United States. Of that amount, coal, natural gas, and petroleum represented 72.721 quadrillion Btu.

265. See 1 A. KAHN, *supra* note 26, at 125; Brief for Appellants at 19, 66-67, *Laclede Gas Co. v. Public Serv. Comm'n*, 600 S.W.2d 222 (Mo. Ct. App. 1980), *appeal dismissed*, 449 U.S. 1072 (1981). The appellants in *Laclede* noted:

As to the evidence, both the staff [Missouri Public Service Commission] witness and the Company [Laclede] witness agreed that advertising promoting the use of gas is beneficial to Laclede and to its customers. . . . Laclede's ability to hold down the cost of gas service to its customers is due in large part to the Company's sustained growth, which growth has and will require advertising support. Increases in sales on Laclede's system produce a greater overall utilization of the system and a spreading of the costs of both the physical facilities and managerial overheads, thus lowering overall unit costs to all customers' benefit.

Id.

266. See Brief for Appellants at 19, *Laclede Gas Co. v. Public Serv. Comm'n*, 600 S.W.2d 222 (Mo. Ct. App. 1980), *appeal dismissed*, 449 U.S. 1072 (1981) (quoting Missouri Public Service Commission Staff witness). Another valid justification for the promotion of gas consumption is that gas is readily storable for future use. See 2 A. KAHN, *supra* note 21, at 120. Since 1975, total gas in storage has ranged from 4,497 billion cubic feet to 6,563 billion cubic feet. See THE ENERGY FACT BOOK, *supra* note 4, at 478. Gas is generally stored in depleted underground geologic formations. See R. PIERCE, G. ALLISON & P. MARTIN, *supra* note 4, at 456. In contrast to gas,

promotes the substantial state interest of economic efficiency. Hence, contrary to recent commission rulings,²⁶⁷ a gas utility's inherent market disadvantage, its benefit to the environment, and consumer economic interests should justify cost allocation of gas promotional advertising.²⁶⁸

Similarly, contrary to recent regulatory commission rulings,²⁶⁹ institutional advertising by gas utilities also deserves cost allocation. Unlike electric utilities, the lustre of the gas utility industry is tarnished by a safety stigma.²⁷⁰ Institutional advertising is a necessary expense for gas utilities to assure actual and potential customers of the safety and reliability of their product.²⁷¹ This expense is an incidence of doing business in a market in which the electricity utility competition does not face a safety stigma. Under *Central Hudson* the gas utility's spe-

electricity is virtually impossible to store economically. See THE ENERGY SOURCE BOOK, *supra* note 4, at 32; R. PIERCE, G. ALLISON & P. MARTIN, *supra* note 4, at 739.

267. See *Re Atlanta Gas Light Co.*, No. 3167-U (Ga. P.S.C. Jan. 10, 1980); *Re Commonwealth Edison Co.*, 35 PUB. UTIL. REP. (PUR) 4th 49 (Ill. Commerce Comm'n 1980); *Re Determination of Whether Advertising Rules Conform to Pub. Util. Regulatory Policies Act of 1978*, No. 35723 (Ind. P.S.C. Jan. 16, 1980); *Re Michigan Gas Utils. Co.*, No. U-6022 (Mich. P.S.C. Feb. 5, 1980); *Re Gas Co.*, 35 PUB. UTIL. REP. (PUR) 4th 106 (N.M.P.S.C. 1980); *Re Minnesota Gas Co.*, 32 PUB. UTIL. REP. (PUR) 4th 1 (S.D.P.U.C. 1979).

268. See notes 263-66 *supra* and accompanying text. Those regulations affecting commercial speech related to fundamental interests have met with court disapproval. See *Carey v. Population Servs. Int'l*, 431 U.S. 678 (1977); note 49 *supra*. Gas utilities have a fundamental right to operate and receive a "fair return" on their investment. See *Smyth v. Ames*, 169 U.S. 466 (1898); notes 54-64 *supra*. Accordingly, regulations that put gas utilities at a distinct disadvantage with respect to interfuel competitors should not be upheld.

269. See, e.g., *Re Commonwealth Edison Co.*, 35 PUB. UTIL. REP. (PUR) 4th 49 (Ill. Commerce Comm'n 1980); *Re Interstate Power Co.*, 32 PUB. UTIL. REP. (PUR) 4th 494 (Minn. P.S.C. 1979); *Re Minnesota Gas Co.*, 32 PUB. UTIL. REP. (PUR) 4th 1 (S.D.P.U.C. 1979); *Re Madison Gas & Elec. Co.*, 34 PUB. UTIL. REP. (PUR) 4th 569 (Wis. P.S.C. 1980).

270. See *Re National Fuel Gas Distribution Corp.*, 17 PUB. UTIL. REP. (PUR) 4th 138, 146-47 (N.Y.P.S.C. 1976) (institutional advertising will be needed to help, among other things, to remove the safety stigma).

This point is poignantly illustrated by the disasters that occurred in Centralia, Missouri, on January 29, 1981 and Zanesville, Ohio, on August 9, 1969. In both instances, a ruptured gas pressure regulator sent high pressure gas of 40 pounds per square inch into low pressure lines designed for four ounces per square inch. *St. Louis Globe-Democrat*, Jan. 29, 1981, at 6, col. 1. As a result, the sudden surge of gas turned pilot lights into "blow torches." *Id.* at col. 3. In the Centralia fire, nine homes were destroyed and 19 others were damaged. *Id.* at col. 6. Property damage was estimated at \$250,000 to \$500,000. *Id.* at col. 2. The Zanesville fire caused \$67,000 damage. *Id.* at col. 6.

271. Institutional advertising to remove a safety stigma should be distinguished from informational advertising purveying safety tips. The former is needed and intended to convince potential customers of the positive qualities of gas use in the home.

cialized need for institutional advertising cost allocation should outweigh any asserted state conservationist, environmental, or economic interest, including benefit to the consumer. Hence, in those situations in which a commission wholly or partially denies institutional advertising cost allocation to electric utilities, it should allow the cost allocation for gas utilities.²⁷²

IV. THE INTERFACE OF *CENTRAL HUDSON* AND *WEST OHIO GAS*

Justice Powell recognized energy conservation as a substantial state interest in *Central Hudson*.²⁷³ In making this observation, the Court followed the current regulatory trend of evaluating the content of the advertisement rather than focusing on the reasonableness of the amount of the expenditure. By endorsing a test based on advertising content, the Court adopted, perhaps unwittingly, a new meaning of "reasonableness."²⁷⁴ The Court, without comment, bypassed constitutional precedent²⁷⁵ and established an analysis not based on the *West Ohio Gas* reasonableness of amount approach.

The *Central Hudson* test raises serious questions and engenders constitutional confusion as to the continued validity of the *West Ohio Gas* reasonableness standard. If the current trend of content regulation is proper, environmental and economic concerns, as well as energy conservation, will qualify as substantial state interests and lead to disallowance of advertising cost allocation, regardless of the reasonableness of the cost's actual amount. Without the benefit of cost allocation, advertising by utilities will portend undesired financial consequences.²⁷⁶ Unwilling to incur economic imprudence voluntarily, utilities may forego advertising altogether. The effect of the *Central Hudson* approach may

272. The Supreme Court has not addressed the issue of cost allocation for goodwill advertising and, in fact, has deliberately skirted it. See *Consolidated Edison Co. v. Public Serv. Comm'n*, 447 U.S. 530 (1980); *Laclede Gas Co. v. Public Serv. Comm'n*, 600 S.W.2d 222 (Mo. Ct. App. 1980), appeal dismissed, 449 U.S. 1072 (1981). The dismissal of the appeal in *Laclede Gas*, however, should not be viewed as an attempt by the Supreme Court to preclude cost allocation of institutional advertising. The specific wording of the dismissal leaves open the possibility for review of this issue at a later time. In fact, a closer inspection of the *Laclede Gas* appeal reveals that the cursory and conclusory opinion of the Missouri Court of Appeals gave the Supreme Court little room to explore the parameters of this issue. Hence, the dismissal of the appeal does not preclude the possibility of eventual Supreme Court review of this issue.

273. *Central Hudson Gas & Elec. Co. v. Public Serv. Comm'n*, 447 U.S. 557, 568 (1980).

274. See notes 102-09 *supra* and accompanying text.

275. See notes 91-101 *supra* and accompanying text.

276. See notes 199-202 *supra* and accompanying text.

promote a "chilling" of commercial speech. In light of these implications, the Supreme court should undertake a thorough reevaluation of *West Ohio Gas* to determine whether the results of the current regulatory trend are desirable.

V. CONCLUSION

Contrary to past practice and policy,²⁷⁷ state regulatory commissions now restrict electric and gas utility advertising either by direct prohibition²⁷⁸ or denial of cost allocation.²⁷⁹ Commissions justify these restrictions on content-based conservationist,²⁸⁰ environmental,²⁸¹ and economic policies.²⁸² Thus, regulatory commissions, aided by state and federal legislative and judicial support,²⁸³ have given the traditional *West Ohio Gas* reasonableness standard²⁸⁴ a new meaning. The reasonableness of utility advertising now depends on its content instead of the amount of its cost.²⁸⁵

In response to these restrictions on advertising, gas and electric utilities recently have raised a first amendment defense under the commercial speech doctrine.²⁸⁶ As a result, utilities have brought into conflict substantial national concerns: the sacrosanct notion of free speech and the nation's interests in energy conservation, environmental protection, and inflation control. The resolution of this conflict depends upon the four-part commercial speech analysis established in *Central Hudson*.²⁸⁷ Under this analysis, a public service commission's direct prohibition of a gas or electric utility's informational, political, institutional, or promotional advertising will violate the first amendment commercial speech doctrine.²⁸⁸

The resolution under *Central Hudson* of the more difficult issue of cost allocation depends on the type of advertising and the nature of the

277. See notes 1 & 94-99 *supra* and accompanying text.

278. See notes 8, 158 & 163-95 *supra* and accompanying text.

279. See notes 9, 159 & 196-271 *supra* and accompanying text.

280. See notes 5, 107 & 208 *supra* and accompanying text.

281. See notes 6, 108 & 209 *supra* and accompanying text.

282. See notes 7, 109 & 210 *supra* and accompanying text.

283. See notes 105-06 *supra* and accompanying text.

284. See notes 91-93 *supra* and accompanying text.

285. See notes 102-09 *supra* and accompanying text.

286. See notes 11, 115 & 157 *supra* and accompanying text.

287. See notes 62-72 *supra* and accompanying text.

288. See notes 163-95 *supra* and accompanying text.

utility speaker. Commissions will not likely permit an electric utility to allocate institutional and promotional advertising.²⁸⁹ Regulatory commissions, however, should allocate both gas and electric utility informational advertising costs to consumer rates.²⁹⁰ Political advertising cost allocation by either gas or electric utilities, though likely to be denied,²⁹¹ may receive protection under the traditional first amendment standard.²⁹² Finally, gas utilities, because of inherent interfuel inequities,²⁹³ should receive special consideration as to institutional and promotional advertising cost allocation.²⁹⁴

The advent of content-based advertising restrictions and the adoption, by the Supreme Court of a content-based policy raises serious questions as to the role and continued validity of the *West Ohio Gas* reasonableness standard. Should the Court reevaluate *West Ohio Gas* and determine that content-based restrictions on advertising are valid, gas and electric utilities will be stripped of any due process or management prerogative defenses.²⁹⁵ These utilities would be left with only the commercial speech doctrine with which to justify advertising and cost allocation. Accordingly, courts and regulatory commissions should consider the inherent inequities of interfuel competition and strive to perform the concededly difficult task of partial allocation to encourage continued use of that advertising which is economically and socially warranted.²⁹⁶

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289. See notes 241-45, 252-53 & 274-76 *supra* and accompanying text.

290. See notes 205-15 *supra* and accompanying text.

291. See notes 219-23 & 231-33 *supra* and accompanying text.

292. See notes 169-85 & 219-23 *supra* and accompanying text.

293. See notes 256-60 *supra* and accompanying text.

294. See notes 173-78 *supra* and accompanying text.

295. See note 10 *supra* and accompanying text.

296. See notes 216-17, 230 & 247 *supra* and accompanying text.

