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Corrupt Power: SEC Sanctions Utility and Sues CEO for Paying Bribes

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Chicago is renowned as the scene of many misdeeds. Only in the "Windy City" is the holiday generally dedicated to expressing affection best remembered for the "St. Valentine's Day Massacre" of a rival group of "rumrunners" during Prohibition. It saw attacks by anti-war protestors at the 1968 Democratic Nominating Convention, when the "Chicago 7" and others chanted "The Whole World is Watching." And there is a veritable "Rogues' Gallery" of political figures who were indicted for criminal acts ranging all the way from non-payment of taxes to statutory rape, namely Congressmen Melvyn Reynolds (Aug. 23, 1995), Dan Rostenkowski (June 1, 1996), Dennis Hastert (April 27, 2012), and Aaron Schock (Nov. 10, 2016), as well as Gov. Rod Blagojevich (Dec. 12, 2008). Nor is this interesting history limited to the public sphere. The chief executive of the Edison affiliate based in Chicago, which became under his reign "Commonwealth Edison," was Samuel Insull, the British emigrant who became one of the holding company titans in the U.S. until his enterprises collapsed during the Depression. Charged with selling worthless stock to unsuspecting investors, he was acquitted by a jury on March 12, 1935, after a seven-week trial. But perhaps the water, as the Chicago River flows backwards, is a causal factor in all of this.

Now, with a plot that sounds more like a political thriller than the real world, Commonwealth Edison (or “ComEd” as it is familiarly known) has worked its way back to center stage. ComEd was acquired in October 2000 as part of the formation of a publicly-traded utility holding company named Exelon, incorporated in Pennsylvania but headquartered in Chicago. Exelon continued to grow, and now is the holding company for six major utility companies in Pennsylvania, New Jersey, Delaware, the D.C. Metro area, and Illinois. On March 12, 2012, Exelon added Constellation Energy, America’s and the world’s leading operator of nuclear power plants, to its portfolio of utility companies. Unfortunately, regulatory strictures on nuclear plants and public fears about their safety made some of the plants too expensive for utility companies to operate and maintain. Government subsidies were frequently needed. Exelon itself has more recently, on Feb. 2, 2022, spun off Constellation Energy, which now operates entirely separately from Exelon. In any event, Exelon is a big company, with reported revenue for the year ended Dec. 31, 2022, of $19 billion and net income of almost $2.2 billion.

Another economic issue facing utilities is the need to obtain governmental approval for the rates charged to customers. For an electric utility like ComEd, that means going before the Illinois Power Board on a regular basis, a process that can prove quite difficult in the face of customer complaints about rising rates, political pressures to respond to the customers, and rising costs for the fuel sources (coal, gas, etc.) that generate electric power at a utility's power plant.

How much more manageable things would be if there were an annual automatic rate adjustment! But that would require enactment of a state law authorizing that result. Further, utilities prefer to take investments in energy efficiency immediately into their rate base in order to set the amounts paid by customers, while amortizing the costs over the useful life of the investment. This generally tends to allow more immediate income, while financial results are reported with only the amount of the annual deduction for the investment cost.

MICHAEL MADIGAN

In the summer of 1966, after completing the first two years of law school, 24-year-old Michael Madigan was hired by the City of Chicago Law Department at the direction of Mayor Richard Daley. Madigan graduated in 1967 and went back to the City Law Department, until leaving to start his own firm in 1972. In 1971 the then 29-year-old

Madigan was elected to the Illinois General Assembly, where he served until 2021. In 1976, he married a divorced woman with a 19-year-old daughter whom he subsequently adopted. That daughter became the Illinois Attorney General in 2003. Meanwhile, Madigan became Speaker of the Illinois General Assembly in 1983, and held that position (except for two years) until Feb. 18, 2021. In 1998, he was chosen as the Chair of the Democratic Party in Illinois and served in that position until his resignation on Feb. 22, 2021. His resignations were followed on March 2, 2022, with an indictment by the U.S. Attorney for the Northern District of Illinois for soliciting and accepting bribes. Clearly, Madigan was a political power in Illinois for decades. What better person to approach to obtain favorable legislation for a business, specifically an electric utility business?

THE CORRUPTION

Three executives of ComEd, including its CEO, Anne Pramaggiore, and a lobbyist, were indicted for undertaking, from 2011 through 2019, to pay various Madigan associates, including a consultant who functioned as a lobbyist, and a law firm, $1.3 million. According to a Sept. 28, 2023 Press Release (the “Press Release”) issued by the Securities and Exchange Commission (“SEC”), the payees “did little to none of the work for which they were hired.” On July 17, 2020, ComEd itself entered into a Deferred Prosecution Agreement (“DPA”) with the U.S. Attorney for the Northern District of Illinois, which provided that ComEd take certain remedial actions for a three year period, as well as paying a $200 million fine. On July 17, 2023, the U.S. Attorney dismissed the charges, as the conditions in the DPA had been met. On May 2, 2023, the three indicted ComEd officials (the CEO, an in-house lobbyist, and the Executive Vice President of legislation and external affairs) and the outside lobbyist were found guilty on all charges after a jury trial.

What exactly did ComEd want? It wanted legislation that would provide additional financial support for nuclear power plants, improved recognition for investments in energy-efficient operating equipment, and most of all, an automatic annual increase in electric rates. According to a Report compiled as of Dec. 1, 2020, by Illinois Public Interest Research Group(“PIRG”), one piece of the key legislative enactments was the 2011 Energy Infrastructure Modernization Act (“EIMA”), which created incentive for creating a so-called “Smart Grid,” as well as granting ComEd automatic rate heights through what PIRG describes as “formula” rate making.

EIMA was set to expire after five years. But with the diligent assistance of Madigan, the 2016 Future Energy Jobs Act (the “FEJA”) was passed. In the words of the SEC’s Sept. 28, 2023 Order Instituting Cease-And-Desist Proceedings and Imposing A Cease-And-Desist

Order (the “Order”), “FEJA renewed the regulatory process that was beneficial to ComEd, ensuring a favorable rate structure.” In the DPA, ComEd “acknowledged that the reasonably foreseeable anticipated benefits to ComEd…[from FEJA] exceeded $150 million.

How did the bribery scheme work? As set out in lengthy detail in the Order, ComEd “arranged for various Madigan associates to obtain jobs, vendor contracts and subcontracts, and monetary payments associated with those jobs and vendor subcontracts.” The SEC asserts that the CEO “signed false and misleading documents in connection with the renewal” of contracts and used “Single Source Justification” forms to justify varying from ComEd’s internal policies. Similarly, ComEd retained a law firm affiliated with Madigan with a commitment to use a minimum of 850 hours of work per year, even if “there was not enough appropriate legal work” to justify that commitment. The Order was issued against both ComEd and its public company parent, Exelon.

The Order reports that the Commission found that Exelon, as the parent of ComEd, had violated Sections 17(a)(2) of the Securities Act of 1933, as amended (the “33 Act”), and 10(b) of the Securities Exchange Act of 1934, as amended (the “34 Act”) as well as rule 10b-5(b) thereunder by engaging in fraudulent conduct in the offer to sell and/or buy securities. The SEC specifically found that Exelon, under Section 8A of the 33 Act and 21C(a) of the 34 Act, as the parent of ComEd, had allowed the misdeeds of ComEd to defraud investors in Exelon. In addition, Exelon was found to have violated Sections 13(b)(2)(A) by failing to keep accurate books and records, and 13(b)(2)(B) for failing to have adequate internal accounting controls.

The Order notes the terms of the DPA and acknowledges the "remedial acts promptly undertaken by [Exelon] and the cooperation afforded the Commission staff." In addition, Exelon had undertaken "to assist the Commission staff in the administration of a distribution plan… to distribute to affected investors" the Fair Fund established from the payment of the civil penalty assessed against Exelon. The Order then imposed on Exelon and ComEd ("Respondents") orders that:

1. Respondents cease-and-desist from future violations of the cited securities laws and regulations; and
2. Exelon pay a civil penalty of $46.2 million within 14 days. The Press Release notes that the SEC investigation was conducted by the Public Finance Abuse Unit of the SEC's Division of Enforcement, and expresses appreciation to the Office of the U.S. Attorney for the Northern District of Illinois.

THE SUIT AGAINST THE CEO

On the same day that the SEC issued the Order, the Commission filed suit against Anne Pramaggiore, the ComEd CEO, in the U.S. District Court for the Northern District of Illinois, Eastern Division. Pramaggiore, a 65-year-old resident of Barrington, Illinois, who earned a law degree from DePaul University, served as the ComEd CEO from March 2012 until May 2018. She received a $100,000 bonus for her efforts to get FEJA passed. The SEC Complaint asserts that Pramaggiore made several false statements during this period, and notes that Exelon sold 446,000 shares of its stock for the Exelon long-term investment plan and 318,000 shares for its employee stock purchase plan. She also signed, at least annually, management representation letters addressed to the outside auditors. These stated:

In addition, on at least two occasions in the fall of 2016, Pramaggiore issued statements which, the SEC charges, were false and misleading. First, in an earnings call on Oct. 26, she said:

At the same time, she was leading the ComEd team to bribe Madigan and have him get FEJA enacted. Then on Nov. 30, she said in a press release regarding the enactment:

She knew the press release was materially misleading because it omitted disclosing the “effort to corruptly influence and reward [Madigan] to secure favorable legislation.”

The Commission charged Pramaggiore with violating Section 17(a)(2) of the 33 Act and Section 10(b) of the 34 Act as well as Rule 10b-5 thereunder, plus a series of violations under Section 13 of the 34 Act and the Rules thereunder, notably including Rule 13a-4 for signing “false and materially misleading certifications pursuant to Section 302 of the Sarbanes-Oxley Act.” These certifications were attached to ComEd’s and Exelon’s quarterly and annual reports filed with the Commission between October 2016 and May 2018. Similarly, Pramaggiore was charged with signing falsified Single Source Justification documents supporting the engagement of Madigan friends and signing false management representation letters to the outside auditors. The SEC requests the Court to:

1. permanently enjoin Pramaggiore from further violations of the cited securities law;
2. order disgorgement of all ill-gotten gains together with prejudgment interest;
3. pay an appropriate civil penalty; and

4. order that she be barred from serving as an officer or director of a public company.

SOME OBSERVATIONS

Considering ComEd’s payment of a $200 million criminal fine as part of the DPA, there is a certain quality of “piling on” in the Commission’s now getting ComEd to pay an additional $46.2 million as a civil fine for basically the same violative conduct. There is no discussion in the Order about the impact of the aggregate of almost a quarter billion dollars on ComEd’s fiscal capacity or the effect the fines may have (if any) on the ComEd customers, i.e., the ratepayers who, according to the December 2020 PIRG Report cited above, had already been forced to pay excessive rates for electric power.

A mitigating factor in favor of the SEC’s enforcement action is that the $46.2 million is to go into a Fair Fund to reimburse affected Exelon investors. One may also wonder why the Commission sued Pramaggiore when she had already been found guilty by a federal jury. We do not know if she has significant personal wealth, although she may. We do not know what her sentence will be as of this blog’s publishing date; sentencing is scheduled for Jan. 16, 2024. We do know that she is appealing her conviction, filing papers to accomplish that on July 23, 2023. It is also reported that she is fighting to preserve her license as an attorney. It may be that the Commission hopes to recover monies from her personally, and also to ensure that she is held accountable at least civilly, even if her criminal conviction is reversed.

In any event, we can be certain that the Commission's request that the Court order a permanent bar on her serving as an officer or director of a public company is of fundamental importance to the SEC.

As Lord Acton famously said:

In this case, it was not the electric power that corrupted, but rather the power of human greed and an exalted sense of importance that not only made Madigan sell his office, but made a utility engage in non-utilitarian fraud.

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