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July 29, 2022

VIA ELECTRONIC MAIL
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board.secretary@bpu.nj.gov

Carmen D. Diaz
Acting Secretary of the Board
Board of Public Utilities
44 South Clinton Avenue, 1st Floor
P.O. Box 350
Trenton, New Jersey 08625-0350

RE: In the Matter of the Petition of Atlantic City Electric Company
for a Declaratory Ruling
BPU Docket No. EO21060893

Dear Acting Secretary Diaz:

Pursuant to the New Jersey Board of Public Utilities' ("Board's" or "BPU's") Order in the above captioned proceeding, Atlantic City Electric Company ("ACE") submits the following compliance items.

On Feb. 24, 2021, Exelon Corporation announced its intention to transfer 100% ownership of Exelon Generation Company, LLC ("ExGen") to a newly created subsidiary that will then be "spun-off" to become ExGen's new, ultimate parent company ("Transaction"). As a result of the Transaction, ExGen and its subsidiaries would no longer be owned by Exelon. On March 30, 2021, ACE filed a letter providing the Board with notice and information about the Transaction ("March 2021 Letter"). In the March 2021 Letter, ACE explained that the Transaction would have no impact on the ownership or control of Exelon or the ownership or control of ACE. ACE asserted that Exelon will continue to be the sole owner of ACE and all other existing Exelon transmission and distribution utilities. After initial discussions with Board Staff, ACE filed a petition on June 7, 2021 seeking a declaratory ruling to confirm that Board approval is not required for the consummation of the spinoff of ExGen from Exelon.

By Order issued November 17, 2021, the Board determined that it was satisfied with the Transaction. The Board made specific findings and also approved the Transaction. Notwithstanding the foregoing, the Board noted that "a continuing obligation to ensure that ACE's customers are protected from . . . possible risks [associated with ACE's corporate framework]." Thus, the Board directed "ACE to, within 180 days following consummation of the Transaction, file an updated Ring Fencing Report and an updated legal opinion."

In compliance with this directive, please see the following. ACE provides the "Atlantic City Electric Company Updated Ring Fencing Report," dated July 29, 2022. (**Attachment 1).** ACE also provides the written Opinion Letter of Ballard Spahr LLP dated July 19, 2022. (**Attachment 2).** With these submissions, ACE respectfully asserts that it has complied with all outstanding separation-related obligations arising from the Board's Order in this docket.

Consistent with the Order issued by the Board in connection with *In the Matter of the New Jersey Board of Public Utilities' Response to the COVID-19 Pandemic for a Temporary Waiver of Requirements for Certain Non-Essential Obligations*, BPU Docket No. EO20030254, Order dated March 19, 2020, these documents are being electronically filed with the Acting Secretary of the Board, the Division of Law, and Rate Counsel. No paper copies will follow.

Thank you for your cooperation and courtesies. Feel free to contact me with any questions.

Respectfully submitted,

Cynthia L.M. Holland

Cynthia L.M. Holland
An Attorney at Law of the
State of New Jersey

Enclosures

cc: Service List

Attachment 1

Ring Fencing Report

Atlantic City Electric Company

Updated Ring Fencing Report

July 29, 2022

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Updated Ring Fencing Report

In June of 2017, Atlantic City Electric Company ("ACE") filed an assessment of Exelon Corporation's ("Exelon" or the "Company") operational and financial risks and the adequacy of the ring-fencing measures agreed to be implemented by Exelon and Pepco Holdings LLC (PHI) as part of their merger consummated on March 23, 2016, to safeguard the financial integrity and stability of PHI and the PHI utilities,[1] including ACE, pursuant to Paragraph 13 of the Joint Recommendation approved by the Board of Public Utilities for the State of New Jersey ("BPU") as part of the MFN Order in Docket No. EM14060581 (the "Ring Fencing Report").[2]

On November 17, 2021, the BPU issued an Order in Docket No. EO21060893, directing ACE to file an updated Ring Fencing Report assessing Exelon's operational and financial risks and the adequacy of existing ring-fencing measures. In its Order, the BPU directed that the report be filed within 180 days following the spin-off of Exelon Generation Company and its subsidiaries from Exelon, which occurred on February 1, 2022.

Pursuant to the BPU's Order of November 17, 2021, ACE hereby provides the following Updated Ring Fencing Report.

I. Introduction

Ring-fencing has been widely used in a number of different industries such as banking, insurance, and public utilities to insulate the credit risk of an issuer of securities from the risks of affiliate issuers within a holding company structure.[3] For utilities, this means separating the activities or assets of the regulated utility from those of the non-regulated business or even other regulated companies owned by the parent company.

The most common functions of ring-fencing are: (a) to make a firm "bankruptcy remote", i.e., to protect the firm from becoming subject to liabilities and other risks associated with the bankruptcy of its affiliated firms; (b) to help ensure that a firm is able to operate on a standalone basis even if its affiliates fail; and (c) to protect a firm from being taken advantage of by its affiliated firms—essentially preserving the business and assets of the ring-fenced firm. [4]

Ring-fencing achieves these goals by restricting or limiting:

- The distressed company's ability to deplete the assets of the subsidiary
- The distressed company's or its creditors' ability to force the utility into bankruptcy
- The ability of a court overseeing the Chapter 11 cases of the distressed company to substantively consolidate the assets and liabilities of the healthy subsidiary with the assets and liabilities of the distressed parent and/or affiliate[5]

Ring-fencing as used in this report refers to the operational and structural isolation of PHI and the PHI utilities from other entities within the Exelon group. The purpose of such isolation is primarily defensive in that it seeks to enable PHI and its utilities to sustain their viability and fulfill their business and financial

[1] The PHI utilities consist of ACE, Potomac Electric Power Company, and Delmarva Power & Light Company.
[2] See In the Matter of the Merger of Exelon Corporation and Pepco Holdings, Inc., BPU Docket No. EM14060581, Order Approving Stipulation of Settlement (the Merger Order) (dated March 6, 2015) and Order Approving Joint Recommendation for Settlement of the Most Favored Nation Issue (the MFN Order)(dated October 31, 2016).
[3] Bonelli, Sharon, Yee, Mona, CFA, and Lapson Ellen, CFA (2003). Corporate Finance, Rating Linkage Within U.S. Utility Groups, Utilities, Holding Companies and Affiliates.
[4] Schwarcz, Steven L., "Ring-Fencing," 2014.
[5] Peterson, Charles and Elizabeth Brereton, "Report on Ring-Fencing," Division of Public Utilities Utah State Department of Commerce. September 2005.

obligations without adverse effects relating to the financial stress of Exelon and affiliate companies. In accordance with the provisions of the Merger Order and the MFN Order, ring fencing requirements were established to protect PHI and the PHI utilities from possible financial distress of Exelon and other Exelon affiliates.

The structure of this report is as follows. First, it begins with an overview of Exelon's risk management framework, designed to identify and estimate the probability that internal and external threats may materialize and prevent the achievement of the Company's objectives. This is followed by a discussion of the key financial and operational risks facing Exelon and an analysis of the principal financial and operating risks inherent in the businesses of Baltimore Gas and Electric Company (BGE), Commonwealth Edison Company (ComEd), and PECO Energy Company (PECO), and their structural separation from the rest of Exelon, particularly PHI and the PHI utilities. Third, the report discusses the key ring-fencing measures that Exelon has put in place to ensure that PHI and the PHI utilities and their customers are protected in the event of financial distress at Exelon or other affiliates. Finally, the report presents legal, credit, and historical evidence from the gas and power utilities sector that supports the Company's view that the ring-fencing measures are adequate and will achieve their stated objectives.

II. Overview of Exelon's Risk Management Framework

Exelon manages enterprise risk for PHI and the PHI utilities in conjunction with Exelon's overall risk management and oversight structure. Exelon's Enterprise Risk Management team, in collaboration with its operating companies, is responsible for coordinating Exelon's risk management program. The program is designed to anticipate strategic and emerging risks, integrate risk into business planning, minimize unexpected performance variances, and support growth initiatives within Exelon's risk appetite. The Enterprise Risk Management team maintains a register of top enterprise risks along with updated information about recent and planned oversight activities to assess management of those risks. It also maintains a register of emerging risks.

Exelon uses the principles articulated in the [Three Lines Model](https://www.theiia.org/globalassets/site/about-us/advocacy/three-lines-model-updated.pdf), developed by the Institute of Internal Auditors (IIA), to guide the allocation of responsibilities among management, internal audit, and enterprise risk management for ownership, governance, and oversight of enterprise risks.[6]

The Enterprise Risk Management team works collaboratively with business teams to identify and assess risks, strengthen risk management practices, and establish risk tolerances that allow for growth while staying within Exelon's risk appetite. It also provides an enterprise-wide view of risks and risk management practices, as well as changes in the risk landscape. Regular risk assessments deepen Exelon's understanding of risks, enable effective action to manage and mitigate risks, and strengthen the company's risk culture. Each operating company, including PHI, has a Risk Management Committee tasked with identifying and evaluating the most significant risks of the business and the actions needed to manage and mitigate those risks.

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[6] The IIA explains the Three Lines Model as follows:

> The Three Lines Model helps organizations identify structures and processes that best assist the achievement of objectives and facilitate strong governance and risk management. The model applies to all organizations and is optimized by:
>
> - Adopting a principles-based approach and adapting the model to suit organizational objectives and circumstances.
> - Focusing on the contribution risk management makes to achieving objectives and creating value, as well as to matters of "defense" and protecting value.
> - Clearly understanding the roles and responsibilities represented in the model and the relationships among them.
> - Implementing measures to ensure activities and objectives ae aligned with prioritized interests of stakeholders.

See: https://www.theiia.org/globalassets/site/about-us/advocacy/three-lines-model-updated.pdf

Senior executives of Exelon regularly discuss enterprise risks with the Audit and Risk Committee of Exelon's Board of Directors, which oversees Exelon's enterprise risk management program. The Exelon Board of Directors also regularly discusses enterprise risks in connection with the evaluation of capital investments, other business opportunities and strategies, as well as emerging trends and developments. PHI executives regularly discuss enterprise risks with the PHI Board of Directors.

III. Overview of Exelon's Financial and Operational Risk Factors

Exelon's risk factors primarily fall within the following categories, which are principally operational and financial in nature and are discussed in detail in Exelon's annual report (*see* Exelon Form 10-K for period ending December 21, 2021, pp. 29-40):

Risks related to market and financial factors primarily include:

- The demand for electricity, reliability of service, and affordability in the markets where the operating companies conduct their business;
- The ability of the operating companies to operate their respective transmission and distribution assets, their ability to access capital markets, and the impacts on their results of operations due to the global outbreak of the 2019 novel coronavirus (COVID-19); and
- Emerging technologies and business models, including those related to climate change mitigation and transition to a low carbon economy.

Risks related to legislative, regulatory, and legal factors primarily include changes to, and compliance with, the laws and regulations that govern:

- Utility regulatory business models;
- Environmental and climate policy; and
- Tax policy.

Risks related to operational factors primarily include:

- Changes in the global climate could produce extreme weather events, which could put the operating companies' facilities at risk, and such changes could also affect the levels and patterns of demand for energy and related services;
- The ability of the operating companies to maintain the reliability, resiliency, and safety of their energy delivery systems, which could affect their ability to deliver energy to their customers and affect their operating costs; and
- Physical and cyber security risks for the operating companies as the owner-operators of transmission and distribution facilities.

Risks related to the separation primarily include:

- Challenges to achieving the benefits of separation; and
- Performance by Exelon and Constellation under the transaction agreements, including indemnification responsibilities.

IV. Limited Risk of Affiliates' Business

There are financial and operating risk factors common to all electric utilities. ACE and all other utility Operating Companies within Exelon are subject to those risk factors, which are essentially the same for each utility. The utility operating companies conduct their respective businesses and operate under governance models and other arrangements and procedures intended to assure that each utility operating company is treated as a separate, independent company, distinct from Exelon and other Exelon subsidiaries in order to isolate it from Exelon and other Exelon subsidiaries in the event of financial difficulty at Exelon or another Exelon subsidiary. These measures insulate each utility from operating and financial risks associated with other utility operations and avoid or limit a downgrade in the credit ratings of any of any utility operating company in the event of a reduction in the credit rating of an affiliate.

Prior to the separation of Exelon's utility businesses from its generation and wholesale trading businesses in February 2022, the generation and wholesale trading businesses were structurally distinct from its parent company, Exelon, which insulated Exelon from the direct effects of an event or claim that might affect the generation or trading business. Exelon's subsidiaries, including PHI, in turn had an additional layer of protection from events in the generation and wholesale trading businesses because of their corporate distinction from Exelon. The corporate separation reduced this limited risk even further, by severing the common ownership of the utilities from the generation and trading businesses.

V. Ring Fencing Measures to Protect PHI Utilities and Their Customers

As discussed in section II of this report, Exelon has put a robust risk management framework in place to ensure that uncertainties are estimated and unknowns are minimized. In the unlikely event that Exelon finds itself in severe financial distress, Exelon, PHI, and ACE have implemented a series of ring-fencing measures with the purpose of protecting PHI and the PHI utilities. Pursuant to the Merger Order and specifically relevant to the state of New Jersey—Exelon, PHI, and ACE have put in place ring-fencing measures designed to:

- Maintain ACE's separate identity and viability so that ACE is capable of running its own business on a standalone basis, as well as avoiding a substantive consolidation with Exelon or Exelon affiliates
- Protect ACE against filing a voluntary bankruptcy petition for any reason other than ACE's individual financial circumstances
- Protect ACE against the risk of defaulting on its own obligations or of losing liquidity due to the financial stress or bankruptcy of its parent or affiliates
- Enhance the Board's regulatory supervision of ACE and its dealings with affiliates

Pursuant to the Merger Order and the MFN Order, ACE and the other Joint Applicants Exelon Corporation, Pepco Holdings, Inc. (now, Pepco Holdings LLC), Exelon Energy Delivery Company, LLC (EEDC) and New Special Purpose Entity, LLC (now PH Holdco LLC, or SPE), (collectively, with ACE, the Companies), provide below the ring-fencing measures relevant to the assessment of the operating and financial risks of ACE. The Joint Applicants implemented the required ring-fencing and corporate governance measures within 180 days following the merger closing and have continued to operate the entities according to these principles, guidelines and requirements set forth in BPU Docket No. EM14060581 since the merger effective date of March 23, 2016. The Joint Applicants acknowledge that the Commission at any time may initiate its own review or investigation regarding ring-fencing measures (or upon petition by any party) and order modifications that it deems to be appropriate, in the public interest and the best interest of ACE customers.

Ring-fencing Measures Relevant to the Assessment of the Operating and Financial Risks of ACE:

Commitment from Merger Order Paragraph #28: ACE will maintain its separate existence as a separate corporate subsidiary and its separate franchises, obligations and privileges.

> Current status: ACE continues to maintain its separate existence as a separate corporate subsidiary and its separate franchises, obligations and privileges.

Commitment from Merger Order Paragraph #29: ACE will maintain separate books and records, and is authorized to maintain those books and records at the corporate headquarters of PHI in Washington, D.C. The Joint Petitioners agree to provide the Board and its Staff and Rate Counsel, upon request, access in New Jersey to ACE's original books and records as maintained in the ordinary course of business within twenty working days after such request. The Joint Petitioners also agree to notify the Board of any material change in the administration, management or condition of ACE's books and records within ten days after the event.

> Current status: The ACE Corporate Governance Principles stipulate that "ACE will maintain separate books and records as required by law and is authorized to maintain those books and records at the corporate headquarters of PHI in Washington, D.C. ACE will maintain separate accounts and financial statements reflecting its separate assets and liabilities. ACE will provide the NJBPU and its Staff and Rate Counsel, upon request, access in New Jersey to ACE's original books and records as maintained in the ordinary course of business within twenty working days after such request. ACE will notify the NJBPU of any material change in the administration, management or condition of ACE's books and records within ten days after the event." ACE maintains its books and records in the required manner.

Commitment from Merger Order Paragraph #30: ACE will not incur or assume any debt, including the provision of guarantees or collateral support, related to this Merger or any future Exelon acquisition.

> Current status: ACE has not incurred or assumed any debt, including the provision of guarantees or collateral support, related to the Merger and will not incur or assume any debt, including the provision of guarantees or collateral support, for any future Exelon acquisition.

Commitment from Merger Order Paragraph #31: Exelon will establish a limited liability company as a special purpose entity ("SPE") for the purpose of holding 100% of the equity interest in PHI.

> Current status: The SPE was established on July 9, 2015, as a special purpose entity for the purpose of holding 100% of the equity interest in PHI. The SPE acquired 100% of the equity interest in PHI on March 23, 2016 and has held 100% of the equity interest in PHI continuously since that date.

Commitment from Merger Order Paragraph #32: The SPE will be a direct subsidiary of Exelon Energy Delivery Company LLC ("EEDC").

> Current status: The SPE was established as a direct subsidiary of EEDC on July 9, 2015 and has remained a direct subsidiary of EEDC continuously since that date.

Commitment from Merger Order Paragraph #33: EEDC will transfer 100% of the equity interest in PHI to the SPE as an absolute conveyance with the intention of removing PHI and its utility subsidiaries from the bankruptcy estate of Exelon and EEDC.

> Current status: On March 23, 2016, EEDC transferred 100% of the equity interest in PHI to the SPE as an absolute conveyance with the intention of removing PHI and its utility subsidiaries from the bankruptcy estate of Exelon and EEDC.

Commitment from Merger Order Paragraph #34: The SPE will have no employees and no operational functions other than those related to holding the equity interests in PHI.

Current status: The SPE has no employees and no operational functions and merely holds the equity interest in PHI.

Commitment from Merger Order Paragraph #35: The SPE shall maintain adequate capital in light of its contemplated business purpose, transactions and liabilities; provided, however, the foregoing shall not require the owners to make any additional capital contributions.

Current status: On March 23, 2016, EEDC transferred to the SPE the entire equity interest in PHI as a contribution to the capital of the SPE. Such contribution to capital of the SPE is adequate in light of the SPE's limited business purpose of holding the entire equity interest in PHI

Commitment from Merger Order Paragraph #36: The SPE will have four directors appointed by EEDC. One of the four SPE directors will be an independent director, who will be an employee of an administration company in the business of protecting SPEs, and must meet the other independence criteria set forth in the SPE governing documents. One other director will be appointed from among the officers or employees of PHI or a PHI subsidiary. The other two SPE directors may be officers or employees of Exelon or its affiliates, including PHI and its subsidiaries.

Current status: As required by the SPE limited liability company agreement, the SPE has four directors appointed by EEDC. One of the four SPE directors is an independent director, who is an employee of an administration company in the business of protecting SPEs, and meets the other independence criteria set forth in the SPE limited liability company agreement. One SPE director is an officer of PHI and ACE. The other two SPE directors are officers of Exelon.

Commitment from Merger Order Paragraph #37: The SPE will issue a non-economic interest in the SPE (a "Golden Share") to an administration company in the business of protecting SPEs and separate from the administration company retained to provide the person to serve as the independent director for the SPE. The holder of the SPE's Golden Share will have a voting right on matters specified in the SPE governing documents, as described below.

Current status: Pursuant to the limited liability company agreement of the SPE, the SPE issued a non-economic interest in the SPE (the "Golden Share") to an administration company in the business of protecting SPEs and separate from the administration company retained to provide the person to serve as the independent director for the SPE. As provided in the limited liability company agreement of the SPE, consent of the holder of the SPE's Golden Share is required on matters specified in the SPE limited liability company agreement.

Commitment from Merger Order Paragraph #39: A voluntary petition for bankruptcy by the SPE will require the affirmative consent of the holder of the Golden Share and the unanimous vote of the SPE board of directors (including the independent director). A voluntary petition for bankruptcy by PHI will require the affirmative consent of the holder of the Golden Share, the unanimous vote of the SPE board of directors (including the independent director), and the unanimous vote of the PHI board of directors. A voluntary petition for bankruptcy for any of PHI's subsidiaries will require the unanimous vote of the PHI board of directors (including its independent directors) and the unanimous vote of the board of directors of the relevant PHI subsidiary.

> Current status: As provided in the limited liability company agreement of the SPE, consent of the holder of the SPE's Golden Share is required on matters specified in the SPE limited liability company agreement. As provided in the limited liability company agreement of PHI, consent of the holder of the SPE's Golden Share is required on matters specified in the PHI limited liability company agreement including voluntary bankruptcy. As provided in the limited liability company agreement of PHI and the bylaws of ACE, a voluntary petition for bankruptcy for ACE requires the unanimous vote of the PHI board of directors (including its independent directors) and the unanimous vote of the board of directors of ACE.

Commitment from Merger Order Paragraph #40: The SPE will maintain arms-length relationships with each of its affiliates and observe all necessary, appropriate and customary company formalities in its dealings with its affiliates. PHI and PHI's subsidiaries will maintain arms-length relationships with Exelon and its affiliates, including the SPE.

> Current status: The SPE has maintained arms-length relationships with each of its affiliates and observed all necessary, appropriate and customary company formalities in its dealings with its affiliates. PHI and PHI's subsidiaries have maintained arms-length relationships with Exelon and its affiliates, including the SPE.

Commitment from Merger Order Paragraph #41: PHI's CEO and other senior officers who directly report to the CEO will hold no positions with Exelon or Exelon affiliates other than PHI and PHI's subsidiaries.

> Current status: PHI's CEO and other senior officers who directly report to the CEO hold no positions with Exelon or Exelon affiliates other than PHI and PHI's subsidiaries.

Commitment from Merger Order Paragraph #42: At all times, the SPE will hold itself out as an entity separate from its affiliates, will conduct business in its own name through its duly authorized directors and officers and comply with all organizational formalities to maintain its separate existence and shall use commercially reasonable efforts to correct any known misunderstanding regarding its separate identity. PHI and its subsidiaries will hold themselves out as separate entities from Exelon and the SPE, conduct business in their own names (provided that PHI and each of PHI's utility subsidiaries may identify itself as an affiliate of Exelon on a basis consistent with other Exelon utility subsidiaries).

> Current status: The SPE, PHI and ACE remain entities separate from their affiliates and continue to operate as described in the commitments referenced above.

Commitment from Merger Order Paragraph #43: The SPE shall maintain its own separate books, records, bank accounts and financial statements reflecting its separate assets and liabilities. PHI and each of PHI's subsidiaries will maintain separate books, accounts and financial statements reflecting its separate assets and liabilities.

> Current status: The SPE limited liability company agreement stipulates that the SPE will maintain separate books, records, bank accounts and financial statements as described in the commitment referenced above. The PHI Corporate Governance Principles and the PHI limited liability company agreement stipulate that PHI will maintain separate books, records, bank accounts and financial statements as described in the commitment referenced above. And the ACE Corporate

Governance Principles stipulate that ACE will maintain separate books, records, bank accounts and financial statements as described in the commitment referenced above. The SPE, PHI and ACE are in compliance with these requirements.

Commitment from Merger Order Paragraph #44: The SPE shall comply with GAAP in all material respects (subject, in the case of unaudited financial statements, to the absence of footnotes and to normal year-end audit adjustments) in all financial statements and reports required of it and issue such financial statements and reports separately from any financial statements or reports prepared for its affiliates; provided that such financial statements or reports may be consolidated with those of its affiliates if the separate existence of the SPE and its assets and liabilities are clearly noted therein.

Current status: The SPE limited liability company agreement stipulates that the SPE shall "comply with GAAP in all material respects (subject, in the case of unaudited financial statements, to the absence of footnotes and to normal year-end audit adjustments) in all financial statements and reports required of it and issue such financial statements and reports separately from any financial statements or reports prepared for its Members or Affiliates; provided that such financial statements or reports may be consolidated with those of its Affiliates if the separate existence of the [SPE] and its assets and liabilities are clearly noted therein." The SPE is in compliance with these requirements.

Commitment from Merger Order Paragraph #45: The SPE shall account for and manage all of its liabilities separately from any other entity, and pay its own liabilities only out of its own funds.

Current status: The SPE limited liability company agreement stipulates that the SPE shall "account for and manage all of its liabilities separately from any other Person, and pay its own liabilities only out of its own funds." The SPE accounts for and manages all of its liabilities separately from any other person and pays its own liabilities out of its own funds.

Commitment from Merger Order Paragraph #46: The SPE shall neither guarantee nor become obligated for the debts of any other entity nor hold out its credit or assets as being available to satisfy the obligations of any other entity.

Current Status: The SPE limited liability company agreement stipulates that the SPE shall "neither guarantee nor become obligated for the debts of any other Person nor hold out its credit or assets as being available to satisfy the obligations of any other Person." The SPE has not guaranteed or become obligated for the debts of any other person and has not and does not hold out its credit or assets as being available to satisfy the obligations of any other person.

Commitment from Merger Order Paragraph #47: Each PHI utility will maintain separate debt and preferred stock, if any, so that none will be responsible for the debts or preferred stock of affiliated companies, and each will maintain its own corporate and debt credit rating as well as ratings for long-term debt and preferred stock, if any. PHI and its subsidiaries will use reasonable efforts to maintain separate credit ratings for their publicly traded securities. PHI will not issue additional long-term debt securities. In particular, PHI shall not rollover or otherwise refinance its currently outstanding long-term debt by issuing new long-term debt. PHI and its utility subsidiaries will use reasonable efforts and prudence to preserve investment grade credit ratings.

Current status: The PHI Corporate Governance Principles stipulate that each PHI utility "will maintain separate debt and preferred stock, if any, so that none will be responsible for the debts or preferred stock of affiliated companies and each will maintain its own corporate and debt credit rating as well as ratings for long-term debt and preferred stock, if any. PHI and the Utilities will use reasonable efforts to maintain separate credit ratings for their publicly traded securities." The PHI Corporate Governance Principles also stipulate that "PHI and the Utilities will use reasonable efforts and prudence to preserve investment grade credit ratings." The non-consolidation opinion stipulates "PHI will not issue additional long-term debt securities. In particular, PHI shall not rollover or otherwise refinance its currently outstanding long-term debt by issuing new long-term debt." The ACE Corporate Governance Principles stipulate that "ACE will maintain separate debt and preferred stock, if any, so that ACE will not be responsible for the debts or preferred stock of affiliated companies, and ACE will maintain its own corporate and debt credit rating as well as ratings for long-term debt and preferred stock, if any. ACE will use reasonable efforts to maintain separate credit ratings for its publicly traded securities." The ACE Corporate Governance Principles also stipulate that "ACE will use reasonable efforts and prudence to preserve investment grade credit ratings." PHI and ACE are in compliance with these requirements.

Commitment from Merger Order Paragraph #48: PHI will not assume liability for the debts of Exelon, the SPE, or any other affiliate of Exelon other than a PHI subsidiary. The PHI subsidiaries will not assume liability for the debts of Exelon, PHI, the SPE, the other PHI subsidiaries, or any other affiliate of Exelon. The SPE shall not acquire, assume or guarantee obligations of any affiliate. PHI will not guarantee the debt or credit instruments of Exelon, the SPE or any other Exelon affiliate other than a PHI subsidiary. The PHI utilities will not guarantee the debt or credit instruments of Exelon, PHI or any other Exelon affiliate including the SPE.

Current status: The PHI Corporate Governance Principles stipulate that "PHI will not guarantee or assume liability for the debts or credit instruments of Exelon, the [SPE], or any other affiliate of Exelon other than a PHI subsidiary." It also stipulates "[the] Utilities will not assume liability for the debts of Exelon, PHI, the [SPE], or any other Exelon affiliate." The SPE limited liability company agreement stipulates that the SPE shall "neither guarantee nor become obligated for the debts of any other Person nor hold out its credit or assets as being available to satisfy the obligations of any other Person" and shall "not acquire, assume or guarantee obligations of any Affiliate". The PHI limited liability company agreement stipulates that PHI "will not guarantee the debt or credit instruments of Exelon, the [SPE] or any other Affiliate of [PHI] other than a [PHI] subsidiary." The PHI Corporate Governance principles stipulate that "The PHI utilities will not guarantee the debt or credit instruments of Exelon, the [SPE], PHI, or any other Exelon affiliate." The SPE, PHI and ACE are in compliance with these requirements.

Commitment from Merger Order Paragraph #49: The SPE shall not pledge its assets for the benefit of any other entity or make loans to, or purchase or hold any indebtedness of, any other entity. The PHI utilities will not pledge or use as collateral, or grant a mortgage or other lien on any asset or cash flow, or otherwise pledge such assets or cash flow as security for repayment of the principal or interest of any loan or credit instrument of, or otherwise for the benefit of, Exelon, PHI or any other Exelon affiliate including the SPE.

Current status: The SPE limited liability company agreement stipulates that the SPE shall "not pledge its assets for the benefit of any other Person or make loans to, or purchase or hold any indebtedness of, any other Person." The PHI Corporate Governance Principles stipulate that "The

Utilities will not pledge or use as collateral, or grant a mortgage or other lien on any asset or cash flow, or otherwise pledge such assets or cash flow as security for repayment of the principal or interest of any loan or credit instrument of, or otherwise for the benefit of, Exelon, the [SPE], PHI or any other Exelon affiliate." The ACE Corporate Governance Principles stipulate that "ACE will not pledge or use as collateral, or grant a mortgage or other lien on any asset or cash flow, or otherwise pledge such assets or cash flow as security for repayment of the principal or interest of any loan or credit instrument of, or otherwise for the benefit of, Exelon, PHI or any other Exelon affiliate." The SPE, PHI and ACE are in compliance with these requirements.

<u>Commitment from Merger Order Paragraph #50:</u> ACE will not include in any of its debt or credit agreements cross-default provisions between ACE securities and the securities of Exelon or any other Exelon affiliate. ACE will not include in its debt or credit agreements any financial covenants or rating-agency triggers related to Exelon or any other Exelon affiliate.

<u>Current status</u>: The ACE Corporate Governance Principles stipulate that "ACE will not include in any of its debt or credit agreements cross-default provisions between ACE securities and the securities of Exelon or any other Exelon affiliate. ACE will not include in its debt or credit agreements any financial covenants or rating agency triggers related to Exelon or any other Exelon affiliate." The PHI Corporate Governance Principles stipulate that "The Utilities will not include in any of their debt or credit agreements cross-default provisions between Utility securities and the securities of Exelon or any other Exelon affiliate …." The ACE credit agreement includes no cross-default provisions between ACE securities and the securities of Exelon or any other Exelon affiliate or financial covenants or rating agency triggers related to Exelon or any other Exelon affiliate.

<u>Commitment from Merger Order Paragraph #51:</u> The SPE will not commingle its funds or other assets with the funds or other assets of any other entity and shall not maintain any funds or other assets in such a manner that it will be costly or difficult to segregate, ascertain or identify its individual funds or other assets from those of its owners or any other person.

<u>Current status</u>: The SPE limited liability company agreement stipulates that the SPE will "not commingle its funds or other assets with the funds or other assets of any other Person, and not maintain any funds or other assets in such a manner that it will be costly or difficult to segregate, ascertain or identify its individual funds or other assets from those of its Members or any other Person." The SPE is in compliance with this requirement.

<u>Commitment from Merger Order Paragraph #52:</u> PHI and its subsidiaries will maintain in its own name all assets and other interests in property used or useful in their respective business and will not transfer its ownership interest in any such property to Exelon or an Exelon affiliate (other than a PHI subsidiary) without requisite approval of the Board of Public Utilities and any approval required under the Federal Power Act; provided that the foregoing shall not limit the ability of PHI to transfer to Exelon or Exelon affiliates any business or operations of PHI or PHI subsidiaries that are not regulated by state or local utility regulatory authorities.

<u>Current status:</u> The PHI limited liability company agreement stipulates that PHI "will maintain in its own name all assets and other interests in property used or useful in its business" and "will not transfer its ownership interest in any such property to Exelon or an Affiliate of Exelon without approval, if required" of the Commission. The PHI Corporate Governance Principles stipulate that

"PHI and each of its subsidiaries will maintain in its own name all assets and other interests in property (including leasehold interests, easements, licenses, beneficial interests, and jointly owned assets) used or useful in their respective business and will not transfer its ownership interest in any such property to Exelon or an Exelon affiliate (other than a PHI subsidiary) without requisite approval of the applicable utility regulatory authority and any approval required under the Federal Power Act; provided that the foregoing shall not limit the ability of PHI to transfer to Exelon or Exelon affiliates any business or operations of PHI or PHI subsidiaries that are not regulated by state or local utility regulatory authorities." The ACE Corporate Governance Principles stipulate that "ACE will maintain ownership in its own name of all assets and other interests in property (including leasehold interests, easements, licenses, beneficial interests, and jointly owned assets) used or useful in its business and will not transfer its ownership of any such property to Exelon or any other Exelon affiliate (other than a ACE subsidiary) without the requisite approval of or notification to the applicable utility regulatory authority and any requisite approval under the Federal Power Act." PHI and ACE are in compliance with these requirements.

Commitment from Merger Order Paragraph #53: The SPE shall ensure that its funds will not be transferred to its owners or affiliates except with the consent and authority of the SPE board of directors.

Current status: The SPE limited liability company agreement stipulates that the SPE shall "ensure that its funds will not be transferred to Exelon or its Affiliates except with the consent and authority of the [SPE board of directors]." All transfers of funds of the SPE have been authorized by the SPE board of directors.

Commitment from Merger Order Paragraph #54: The SPE shall ensure that title to all real and personal property acquired by it is acquired, held and conveyed in its name.

Current status: The SPE limited liability agreement stipulates that the SPE shall "ensure that title to all real and personal property acquired by it [is] acquired, held and conveyed in its name." The SPE maintains all of its assets in its own name.

Commitment from Merger Order Paragraph #55: No entities other than PHI and its subsidiaries, including the PHI utilities and PHI Service Company ("PHISCo"), will participate in the PHI utilities' money pool. The PHI utilities will not participate in any money pool operated by Exelon, and there will be no commingling of the PHI money pool funds with Exelon. Any deposits into or loans through the PHI money pool by PHI utilities shall be on terms no less favorable than the depositor or lender could obtain through a short-term investment of similar funds with independent parties. Any borrowings from the PHI money pool by a PHI utility shall be on terms no less favorable and cost effective than the PHI utility could obtain through short-term borrowings from (including sales of commercial paper to) independent parties. Exelon will give notice to the Board of Public Utilities within seven days in the event that any participant in the PHI money pool is rated below investment grade by any of the three major credit rating agencies. The documents and instruments creating the PHI money pool (and any modifications thereof) will be subject to approval by the Board of Public Utilities. The Board of Public Utilities may revoke the right of ACE to participate in the PHI money pool or require a modification in order for ACE's continued full or partial participation.

Current Status: The ACE Corporate Governance Principles stipulate "ACE will not participate in any money pool arrangement other than a money pool with PHI and its subsidiaries (including the Utilities and PHI Service Company), and there will be no commingling of ACE funds with Exelon.

Any deposits into or loans through the PHI money pool by ACE shall be on terms no less favorable than the depositor or lender could obtain through a short-term investment of similar funds with independent parties. Any borrowings from the PHI money pool by ACE shall be on terms no less favorable than ACE could obtain through short-term borrowings from (including sales of commercial paper to) independent parties. ACE will cause Exelon to give notice to the NJBPU within seven business days in the event that any participant in the PHI money pool is rated below investment grade by any of the three major credit rating agencies." The PHI Corporate Governance Principles stipulate "No entities other than PHI and its subsidiaries (including the Utilities and PHI Service Company) will participate in the PHI money pool. The Utilities will not participate in any money pool operated by Exelon, and there will be no commingling of funds with Exelon. Any deposits into or loans through the PHI money pool by the Utilities shall be on terms no less favorable than the depositor or lender could obtain through a short-term investment of similar funds with independent parties. Any borrowings from the PHI money pool by a Utility shall be on terms no less favorable than the Utility could obtain through short-term borrowings from (including sales of commercial paper to) independent parties."

On October 31, 2016 the NJBPU issued its Order Approving Joint Recommendation for the Settlement of the Most Favored Nation Issue in Docket No. EM14060581. This settlement contained approval by the BPU of the changes to the money pool documents required by the merger settlement. These changes were filed with FERC on November 7, 2016 and ACE is in compliance the requirements related to the money pool.

Commitment from Merger Order Paragraph #57: PHI subsidiaries, other than PHISCo and the PHI utilities, that are currently engaged in operations that are not regulated by a state or local utility regulatory authority will be transferred to Exelon or an Exelon affiliate; provided that PHI may retain ownership of Conectiv LLC ("Conectiv") as a holding company for ACE and Delmarva Power; and Conectiv or subsidiaries of Conectiv may retain ownership of real estate and other assets that are used in whole or in part in the business of the PHI utilities. Post-Merger, PHI will not initiate or invest in new non-utility operations without first obtaining Board approval in a written order. Following the closing of the Merger, ACE may, without further approval of the Board, become a direct subsidiary of PHI, rather than remain a direct subsidiary of Conectiv. If ACE does not become a direct subsidiary of PHI, ACE will, in its first post-merger base rate case, justify and support that it is in the public interest for it to remain as a direct subsidiary of Conectiv rather than a direct subsidiary of PHI. Notwithstanding the requirements of this Paragraph or the requirements of Paragraphs 48, 49 and 50, ACE may continue existing arrangements related to the obligations of Atlantic City Electric Transition Funding LLC.

Current status: On March 23, 2016, PHI subsidiaries, other than PHISCo and the PHI utilities and subsidiaries of the PHI utilities, were transferred to Exelon or an Exelon affiliate. The 50% ownership interest in Millennium Account Services LLC was transferred to PHI. PHI elected to hold the stock of Delmarva and ACE directly, and ceased the use of Conectiv as a holding company.

Commitment from Merger Order Paragraph #58: The SPE will maintain a separate name from and will not use the trademarks, service marks or other intellectual property of Exelon, PHI, or PHI's subsidiaries. PHI and its utility subsidiaries will each maintain a separate name from and will not use the trademarks, service marks or other intellectual property of Exelon or its other affiliates, except that PHI and each of PHI's utility subsidiaries may identify itself as an affiliate of Exelon on a basis consistent with other Exelon utility subsidiaries.

Current status: The SPE limited liability company agreement stipulates that the SPE will "not use the trademarks, service marks or other intellectual property of any of its Affiliates". The PHI limited liability company agreement stipulates that PHI "shall maintain a separate name from and will not use the trademarks, service marks or similar intellectual property of Exelon or other Affiliates of Exelon, except that [PHI] may identify itself as an Affiliate of Exelon on a basis consistent with utility Subsidiaries of Exelon." The PHI Corporate Governance Principles stipulate that "PHI and the Utilities will each maintain a separate name from and will not use the trademarks, service marks or other similar intellectual property of Exelon or its other affiliates, except that PHI and each Utility may identify itself as an affiliate of Exelon on a basis consistent with other Exelon utility subsidiaries." The ACE Corporate Governance Principles stipulate that "ACE will maintain a separate name from and will not use the trademarks, service marks or other similar intellectual property of Exelon or its other affiliates, except that ACE may identify itself as an affiliate of Exelon on a basis consistent with other Exelon utility subsidiaries." The SPE, PHI and ACE are in compliance with these requirements.

Commitment from Merger Order Paragraph #59: Any amendment to the organizational documents of the SPE that would remove or alter the voting or other ring-fencing requirements described above will require the unanimous vote of the board of directors of the SPE, including the independent director, and the affirmative consent of the holder of the Golden Share.

Current status: The SPE operating agreement stipulates "neither the Members nor the Board nor any Director nor any Officer nor any other Person shall be authorized or empowered, nor shall they permit the [SPE], without (i) the unanimous prior approval of the [SPE] Board, including the Independent Director, and (ii) the prior written consent of the [holder of the Golden Share], to … (H) modify the provision of Section 5.1(a); or (I) remove the unanimous consent requirement set forth above in this Section 5.1(b)." The non-consolidation opinion notes that "any amendment to the organizational documents of [the SPE] that would remove or alter the voting or other ring-fencing requirements described above requires the unanimous vote of the board of directors of [the SPE], including the independent director, and the affirmative consent of the holder of the Golden Share."

Commitment from Merger Order Paragraph #60: Within 180 days following completion of the Merger, Exelon will obtain a legal opinion in customary form and substance and reasonably satisfactory to the Board of Public Utilities, to the effect that, as a result of the ring-fencing measures it has implemented for PHI and its subsidiaries, a bankruptcy court would not consolidate the assets and liabilities of the SPE with those of Exelon or EEDC, in the event of an Exelon or EEDC bankruptcy, or the assets and liabilities of PHI or its subsidiaries with those of either the SPE, Exelon or EEDC, in the event of a bankruptcy of the SPE, Exelon or EEDC. In the event that such opinion cannot be obtained, Exelon will promptly implement such measures as are required to obtain such opinion.

Current status: The required legal opinion was obtained by Exelon and filed with the Commission on June 29, 2016.

Commitment from Merger Order Paragraph #61: ACE will not pay dividends to its parent company if, immediately after the dividend payment, its common equity level would fall below 48%, as equity levels are calculated under the ratemaking precedents of the Board of Public Utilities.

Current status: Each quarter since the merger, notice has been filed with the Board of Public Utilities of dividends paid by ACE to its parent and showing ACE's equity ratio after the dividend payment did not fall below 48% as calculated under rate making precedents of the Board of Public Utilities.

Commitment from Merger Order Paragraph #62: ACE shall not make any distribution to its parent if ACE's corporate issuer or senior unsecured credit rating, or its equivalent, is rated by any of the three major credit rating agencies below investment grade.

Current status: ACE's corporate issuer and senior unsecured ratings remain above investment grade.

Commitment from Merger Order Paragraph #63: ACE shall file with the Board of Public Utilities, within 5 business days after the payment of a dividend, the calculations that it used to determine the equity level at the time the board of directors considered payment of the dividend and the calculations to demonstrate that the common equity ratio immediately after the dividend payment did not fall below 48%, as equity levels are calculated under the ratemaking precedents of the Board of Public Utilities.

Current status: Each quarter since the merger, notice has been filed with the Board of Public Utilities of dividends paid by ACE to its parent and showing ACE's equity ratio after the dividend payment did not fall below 48% as calculated under rate making precedents of the Board of Public Utilities.

Commitment from Merger Order Paragraph #65: At the time the SPE is formed and every year thereafter, ACE shall provide the Board of Public Utilities with a certificate from an officer of Exelon certifying: (a.) Exelon shall maintain the requisite legal separateness in the corporate reorganization structure; (b.) the organization structure serves important business purposes for Exelon; and (c.) Exelon acknowledges that subsequent creditors of PHI and ACE may rely upon the separateness of PHI and ACE and would be significantly harmed in the event separateness is not maintained and a substantive consolidation of PHI or ACE with Exelon were to occur.

Current status: Each year since the merger, the compliance certificates have been filed with the Board.

Commitment from Merger Order Paragraph #66: Exelon shall not, without prior Board of Public Utilities approval, alter the corporate character of EEDC to become a functioning corporate entity providing common support services for PHI utilities.

Current status: The second amendment to second amended and restated limited liability company agreement for EEDC stipulates that "[Exelon] shall not, without prior approval of … the New Jersey Board of Public Utilities …, alter EEDC's corporate character to become a functioning corporate entity providing common support services for EEDC utilities."

Commitment from Merger Order Paragraph #67: Exelon shall not engage in an internal corporate reorganization relating to the SPE, PHI or ACE, or EEDC for which Board of Public Utilities approval is not required without 90 days prior written notification to the Board of Public Utilities. Such notification shall include: (a) an opinion of reputable bankruptcy counsel that the reorganization does not materially impact the effectiveness of PHI's existing ring-fencing; or (b) a letter from reputable bankruptcy counsel describing what changes to the ring-fencing would be required to ensure PHI is at least a effectively ring-fenced following the reorganization and a letter from Exelon committing to obtain a new non-consolidation option following the reorganization and to take any further steps necessary to obtain such an opinion. Exelon will not object if the Board of Public Utilities elects to open an investigation into the matter if the Board of Public Utilities deems it appropriate. Notwithstanding the above language in this Paragraph, the Joint Petitioners shall not materially alter the ring-fencing plan described in this stipulation agreement without first obtaining approval in a written order from the Board of Public Utilities.

> Current status: The limited liability company agreement for EEDC stipulates that "The Member shall not approve or engage in an internal corporate reorganization relating to the Company, … PHI … or ACE for which the applicable Commission approval is not required without 90 days prior written notification to such Commission. Such notification(s) shall include: (a) an opinion of reputable bankruptcy counsel that the reorganization does not materially impact the effectiveness of … ACE's existing ring-fencing; or (b) a letter from reputable bankruptcy counsel describing what changes to the ring-fencing would be required to ensure … ACE is at least as effectively ring-fenced following the reorganization and a letter the Member committing to obtain a new non-consolidation option following the reorganization and to take any further steps necessary to obtain such an opinion. The Member will not object if the Commission elects to open an investigation into the reorganization if such Commission deemed it appropriate." Under the Commission's order approving the merger, the Joint Applicants shall not materially alter the ring-fencing plan described in the order without first obtaining approval in a written order from the Commission.

Commitment from Merger Order Paragraph #68: None of the cost of establishing, operating or modifying the SPE will be borne by ACE or its distribution customers. The cost of obtaining the opinion of legal counsel referred to in Paragraphs 60 and 67 (or any future opinion) will not be borne by ACE or its distribution customers.

> Current status: No part of the cost of establishing, operating or modifying the SPE has been charged or allocated to ACE or its distribution customers. The cost of obtaining the opinion of legal counsel has not been charged or allocated to ACE or its distribution customers. The cost of obtaining any future opinion of counsel will not be borne by ACE or its distribution customers.

Commitment from MFN Order Paragraph #12: ACE shall maintain a rolling 12-month average annual equity ratio of at least 48%. ACE will not pay dividends to its parent company if, immediately after the dividend payment, its common equity level would fall below 48%, as equity levels are calculated under the ratemaking precedents of the Board.

> Current Status: The ACE Corporate Governance Principles stipulate that "ACE shall maintain a rolling 12-month average annual equity ratio of at least 48 percent. ACE will not pay dividends to its parent company if, immediately after the dividend payment, its common equity level would fall below 48 percent, as equity levels are calculated under the ratemaking precedents of the NJBPU."

Commitment from MFN Order Paragraph #14: The Joint Petitioners agree to implement the ring-fencing and corporate governance measures set out above within 180 days of merger closing for the purpose of providing protections to customers. Five years after the closing of the Merger, the Joint Petitioners shall have the right to review the provisions contained in Paragraphs 28 through 70, and to make a filing with the Board of Public Utilities requesting authority to modify or terminate those provisions. Notwithstanding such right, Joint Petitioners agree not to proceed with any such modification or termination without first obtaining Board approval in a written order. In addition, the Parties recognize that the Board at any time may initiate its own review or investigation regarding ring-fencing measures (or upon petition by any party) and order modifications that it deems to be appropriate, in the public interest and the best interest of ACE customers.

> Current status: The Joint Applicants implemented the required ring-fencing and corporate governance measures within 180 days following the merger closing. The Joint Applicants recognize it has been over 5 years since the merger, but have not requested any changes to the ring-fencing measures and acknowledge that the Commission at any time may initiate its own review or investigation regarding ring-fencing measures (or upon petition by any party) and order modifications that it deems to be appropriate, in the public interest and the best interest of ACE customers.

VI. Assessment of Adequacy of Ring-Fencing Measures

Exelon believes that the ring-fencing measures put in place are adequate and effectively separate PHI and the PHI utilities from any adverse effects relating to ownership by Exelon and the risks of Exelon's other utility or non-utility businesses. PHI and the PHI utilities will be protected and able to continue meeting their business and financial needs even in a scenario of extreme circumstances resulting in Exelon's bankruptcy.

This view is supported by the law firm Ballard Spahr as laid out in its Non-Consolidation Opinion, by the three credit rating agencies, and by the historical examples in the electric and gas utilities sector.

i. Ballard Spahr's Non-Consolidation Opinion

In its Non-Consolidation Opinion filed concurrently, Ballard Spahr (Ballard) states that in Ballard's opinion there would be no reasonable likelihood of substantive consolidation of the PHI utilities with Exelon and its affiliates, in the event that Exelon and/or its affiliates were to become a debtor in bankruptcy. Below are the key excerpts from the Non-Consolidation Opinion:[7]

(1) in a properly presented and argued proceeding in a case under the Bankruptcy Code in which Exelon and/or EEDC were a debtor, a United States bankruptcy court of competent jurisdiction would not, under applicable federal bankruptcy law, apply the doctrine of substantive consolidation to consolidate the assets and liabilities of PH Holdco with the assets and liabilities of such debtor; and

(2) in a properly presented and argued proceeding in a case under the Bankruptcy Code in which PH Holdco, Exelon and/or EEDC were a debtor, a United States court of competent jurisdiction would not, under applicable federal bankruptcy law, apply the doctrine of substantive consolidation to

[7] Non-Consolidation Opinion, page 29.

consolidate the assets and liabilities of Pepco Holdings or the Pepco Holdings Utilities with the assets and liabilities of such debtor

ii. Credit Rating Agencies

The purpose of credit ratings is to provide investors with a grading system by which future relative creditworthiness of securities may be measured. Although different rating agencies may use different rating symbols, each rating agency aims to rate individual companies in such a way that companies and securities with the same rating letter have an equivalent default risk level.

To assess the impact of the merger on the PHI utilities' creditworthiness, it is useful to observe how the credit rating of the PHI utilities changed as a result of the merger. If the Exelon-PHI merger had resulted in a higher risk of default for the PHI utilities because of the business risks of Exelon, then a downgrade in the PHI utilities' credit rating would have been expected post-merger. However, the long-term credit rating of the PHI utilities did not change as a result of the merger. In other words, the merger did not expose the PHI utilities or their customers to any additional financial risks. This is due, in part, to the robust ring-fencing measures put in place. Furthermore, since the merger, there has been improvement in credit ratings at the PHI utilities as shown in Table 1.

Moreover, these ring-fencing measures closely resemble those that are in place for RF Holdco and BGE, and as a result, rating agencies are treating PHI and its subsidiaries similarly to the way they treat RF Holdco and BGE. The rating agencies attribute a significant degree of confidence to the effectiveness of the ring-fencing. This explains why they have not constrained the credit rating of the PHI utilities to be identical to the rating of Exelon.

Standard & Poor's Rating Services (S&P) rates the PHI utilities at one notch higher than parent Exelon. Specifically to ACE, S&P notes that ACE's "structural and regulatory protections provide a degree of insulation from parent Exelon."[8] Given the existence of insulation, ACE's current stand-alone credit profile of "A-" and its issuer credit rating of 'A-' are one notch higher than Exelon's group credit profile of 'BBB+'.

S&P notes that the one notch differential between ACE and Exelon is based on all the following conditions being met:

- The subsidiary's stand-alone credit profile is higher than the group credit profile (i.e., parent company);
- The subsidiary's financial performance and funding prospects are highly independent from those of the group, so that even if other core entities encounter severe setbacks, the relative strength of the subsidiary would remain nearly intact;
- The subsidiary is severable from the group, in S&P's opinion, and able to stand on its own or subcontract certain functions previously provided by the parent;
- The parent's strategy with respect to the subsidiary is clear and, in particular, the parent has a compelling economic incentive to preserve the subsidiary's credit strength;
- It is unlikely, in S&P's opinion, that the subsidiary will be drawn into bankruptcy proceedings at the group level that would lead to a default on the subsidiary's obligations;

[8] S&P Global Ratings, Atlantic City Electric Co., January 18, 2022, page 1.

- For regulated entities, there is evidence that legislative, regulatory, or structural restrictions would inhibit the subsidiary from supporting the group to an extent that would in turn unduly impair the subsidiary's stand-alone creditworthiness;[9]

In essence, S&P believes that the ring-fencing measures in place are adequate in insulating ACE from parent-level and affiliate-level activity, and hence this justifies a one notch separation above the parent's rating.

Moody's Investor Service and Fitch Ratings—the other two rating agencies in the U.S.—apply their own criteria on a case-by-case basis. Overall, however, the three sets of criteria are largely similar, and so have been the agencies' risk assessments. Following the merger announcement, all three rating agencies affirmed the credit rating of each PHI utility. As of the filing of this report, these credit ratings have remained stable. [10] The Company interprets such actions to indicate that the agencies are confident that the ring-fencing effectively provides a substantial degree of separation between the PHI utilities and Exelon.

On February 1, 2022, Exelon completed the separation from Constellation Energy Corp., Exelon's former power generation and competitive energy business. With the separation completed, Exelon is now a large, fully regulated, transmission and distribution utility holding company serving more than 10 million customers. As a result of this transformation to a fully regulated business, S&P "revised [its] assessment of Exelon's business risk profile to excellent from strong reflecting the improved business risk."[11]

Conclusion

Exelon conducts enterprise-wide and operating company-specific risk assessments to identify and focus on the top risks facing the Company through a best-in-class Enterprise Risk Management framework. In the unlikely event that the materialization of risks may lead to financial distress at Exelon, the Company is confident that PHI and the PHI utilities would not be impacted as ring-fencing measures have been put in place to protect them and their customers.

Ring-fencing represents a proven way of protecting a regulated utility and its customers from potential risks of financial harm from its affiliated companies. Exelon is confident that the ring-fencing measures established will effectively separate PHI and the PHI utilities from any adverse effects relating to ownership by Exelon and the risks of Exelon's other utility or non-utility businesses.

External stakeholders support this view. Ballard Spahr in its Non-Consolidation Opinion has stated that there would be no reasonable likelihood of substantive consolidation of the PHI utilities' assets with those of Exelon in the event that Exelon were to become a debtor in bankruptcy. Similarly, credit rating agencies have indicated that they have confidence that the ring-fencing will separate the credit of the PHI utilities from that of Exelon.

Finally, the Company is confident that the ring-fencing measures put in place to protect PHI and the PHI utilities continue to represent the leading edge in utility ring-fencing and that they will become the utility industry standard for providing the highest degree of protection going forward.

[9] Excerpt from S&P's methodology on credit ratings.
[10] See Table 1 in the Appendix.
[11] S&P Global Ratings, Exelon Corporation, February 2, 2022, page 1.

Appendix

Table 1: Comparison of the Credit Ratings of Pepco Holdings Utilities Before the Merger Announcement and Since the Merger Completion

	S&P		Moody's		Fitch	
	Before*	2022**	Before*	2022**	Before*	2022**
Atlantic City Electric - LT	BBB+	A-	Baa2	Baa1	BBB	BBB+
Delmarva Power & Light - LT	BBB+	A-	Baa1	Baa1	BBB+	BBB+
Potomac Electric Power - LT	BBB+	A-	Baa1	Baa1	BBB	BBB+

*Ratings as of Sept 10, 2014

**Ratings as of June 1, 2022

Attachment 2

Ballard Spahr Opinion

Ballard Spahr LLP

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July 19, 2022

Exelon Corporation
10 South Dearborn Street
Chicago, Illinois 60680-5379

PH HoldCo LLC and
Pepco Holdings LLC
701 Ninth Street NW
Washington, DC 20068

Re: Substantive Consolidation – PH Holdco LLC and Pepco Holdings

Ladies and Gentlemen:

We have acted as counsel to Exelon Corporation, a Pennsylvania corporation ("Exelon") and PH Holdco LLC, a Delaware limited liability company ("Holdco"), for the limited purpose of opining as to whether, in a properly presented and argued proceeding in a case under Title 11 of the United States Code (the "Bankruptcy Code") in which (i) Exelon and/or Exelon Energy Delivery Company LLC, a Delaware limited liability company ("EEDC," and collectively with Exelon, the "Exelon Entities"), were a debtor, a bankruptcy court of competent jurisdiction would, under applicable federal bankruptcy law, apply the doctrine of substantive consolidation to consolidate the assets and liabilities of Holdco with the assets and liabilities of such debtor or (ii) one of the Exelon Entities or Holdco was a debtor, a bankruptcy court of competent jurisdiction would, under applicable federal bankruptcy law, apply the doctrine of substantive consolidation to consolidate the assets and liabilities of Holdco, Pepco Holdings LLC (formerly Pepco Holdings, Inc.), a Delaware limited liability company ("Pepco Holdings"), Atlantic City Electric Company, a New Jersey corporation ("ACE"), Delmarva Power & Light Company, a Delaware and Virginia corporation ("Delmarva"), and Potomac Electric Power Company ("Pepco," and together with ACE and Delmarva, the "Pepco Holdings Utilities") with the assets and liabilities of such debtor.

This opinion may be relied upon by you and may not be used or relied upon by any other persons for any other purpose, without in each instance our prior written consent; provided, however, that Moody's Investors Service, Inc., Standard & Poor's Ratings Services and Fitch Inc. may rely on this opinion as if it were addressed to them. You may also furnish copies hereof (i) to your independent auditors, advisors and attorneys; (ii) upon the request of any state or federal authority or official having regulatory jurisdiction over you; and (iii) pursuant to order or legal process of any court or governmental agency.

I. FACTS AND ASSUMPTIONS

In rendering the opinions set forth herein, we have made such examination and investigation as we have deemed relevant or necessary as the basis for the opinions set forth below, including an examination of originals or copies, certified or otherwise identified to our satisfaction, of the agreements and other documents specifically described herein by name and date and inquiries of officers and representatives of the Exelon Entities, Holdco, Pepco Holdings and the Pepco Holdings Utilities. We have relied upon, and assumed the accuracy of, certificates and other documents and records furnished or made available to us, and statements made, in response to our inquiries with respect to the factual matters set forth herein by officers of Exelon Entities, Holdco, Pepco Holdings and the Pepco Holdings Utilities. We have assumed (i) the genuineness of all signatures, (ii) the authenticity of all documents submitted to us as originals, (iii) the conformity to original documents of all documents submitted to us as certified, conformed or photostatic copies, and (iv) that the following facts and assumptions in this Part I are true on the date hereof and will remain true at all other times relevant to this opinion. In addition, we assume that Exelon Entities, Holdco, Pepco Holdings and the Pepco Holdings Utilities have been and will continue to be in compliance with all of the laws, regulations, orders and agreements referred to in this Part I in all material respects and to the extent relevant to this opinion letter.

A. The Merger & the Separation

1. The Merger

On April 29, 2014, Exelon and Pepco Holdings, Inc. executed an Agreement and Plan of Merger (as subsequently amended and restated as of July 18, 2014) to combine the two companies in an all cash transaction. On March 23, 2016, following the receipt of all required regulatory approvals, Exelon and Pepco Holdings, Inc. consummated the merger of Pepco Holdings, Inc. with a Purple Acquisition Corp. (the "Merger").

Prior to consummation of the Merger, the board of directors of Pepco Holdings, Inc. authorized the conversion of Pepco Holdings, Inc. into a limited liability company pursuant to Section 266 of the General Corporation Law of the State of Delaware and Section 18-214 of the Limited Liability Company Act of the State of Delaware (the "Conversion"). Following consummation of the Merger, the Conversion was approved by Exelon and EEDC as the sole shareholders of Pepco Holdings, Inc. Pepco Holdings, Exelon and EEDC caused to be filed with the Secretary of State of Delaware the Certificate of Conversion and the Certificate of Formation required by Section 18-214(b) of the Act, and the Conversion has become effective.

2. The Separation

On February 1, 2022, Exelon completed (i) the transfer of the membership interests of the Constellation Energy Generation, LLC (formerly known as Exelon Generation Company, LLC) to Constellation Energy Corporation ("Constellation") and (ii) the pro rata distribution of the capital stock of Constellation to the holders of Exelon's common stock on February 1, 2022 (the "Separation"). The consummation of the Separation did not affect any of the legal separateness provisions currently in place between the Exelon Entities, Pepco Holdings and the Pepco Holdings Utilities, which are described in more detail below.

B. Ring-Fencing Measures

In connection with the Merger approval proceedings, the Exelon Entities and Pepco Holdings committed to implement the following measures (the "Ring-Fencing Measures"):

1. Exelon and EEDC established Holdco as a special purpose limited liability company for the purpose of holding 100% of the equity interest in Pepco Holdings.

2. Holdco is direct subsidiary of EEDC and an indirect subsidiary of Exelon.

3. Immediately following the closing of the Merger, EEDC transferred 100% of the equity interest in Pepco Holdings to Holdco with the intention of removing Pepco Holdings and the Pepco Holdings Utilities from the bankruptcy estate of Exelon and EEDC.

4. Pepco Holdings holds 100% of the equity of the Pepco Holdings Utilities.

5. Holdco has no employees and no operational functions other than those related to holding the equity interests in Pepco Holdings.

6. Holdco has adequate capitalization in light of its contemplated business purpose; provided, however, that the Exelon Entities will not be required to make any additional capital contributions to Holdco.

7. Holdco is restricted under the PH Holdco Amended and Restated Limited Liability Company Operating Agreement (the "Holdco Operating Agreement") to performance of certain limited activities in compliance with its special purpose status. In addition, the Holdco Operating Agreement contains legal separateness provisions, as more fully described in Section I.C. below.

8. Holdco has four directors appointed by EEDC. One of the four directors is an independent director, who is an employee of an administration company in the business of protecting special purpose entities, and meets the other independence criteria set forth in the Holdco Operating Agreement. One other director was appointed from among the officers or

employees of Pepco Holdings or a subsidiary of Pepco Holdings. The other two directors are officers or employees of Exelon or its affiliates, including Pepco Holdings and its subsidiaries.

9. The consent of Holdco's independent director is required in order for Holdco or Pepco Holdings to initiate a voluntary bankruptcy, insolvency, dissolution, reorganization, liquidation or any other similar proceeding.

10. Holdco has issued a non-economic share to GSS Holdings (PH Utility), Inc. ("Member B") for the sole and limited purpose of restricting the right of Holdco to take certain bankruptcy-related actions.

11. Pepco Holdings' Amended and Restated Limited Liability Company Operating Agreement (the "Pepco Holdings Operating Agreement") contains legal separateness provisions, as more fully described in Section I.D. below.

12. Pepco Holdings has a board of directors consisting of seven or more people. A majority of the members of the Pepco Holdings board of directors must be "independent" (as defined by New York Stock Exchange rules). Of the remaining directors, at least one must be selected from among the officers or employees of Pepco Holdings or a Pepco Holdings subsidiary.

13. Pepco Holdings' chief executive officer and other senior officers who directly report to Pepco Holdings' chief executive officer will hold no positions (i.e., as directors, officers or employees) with Exelon or Exelon affiliates other than Pepco Holdings and Pepco Holdings' subsidiaries.

14. The Pepco Holdings Operating Agreement requires approval of the its entire board of directors to: (a) commence any case, proceeding or other action on behalf of Pepco Holdings under any existing or future law of any jurisdiction relating to bankruptcy, insolvency, reorganization, or relief for debtors; (b) institute proceedings to have Pepco Holdings adjudicated as bankrupt or insolvent; (c) consent to or acquiesce in the institution of bankruptcy or insolvency proceedings against Pepco Holdings; (d) file a petition or consent to a petition seeking reorganization, arrangement, adjustment, winding-up, dissolution, composition, liquidation, or other relief on behalf of Pepco Holdings of its debts under any federal or state law relating to bankruptcy; (e) apply for, or consent to, or acquiesce in the appointment of, a receiver, liquidator, sequestrator, trustee or other officer with similar powers of such person with respect to Pepco Holdings; (f) make any assignment for the benefit of the Pepco Holdings' creditors; (g) admit in writing Pepco Holdings' inability to pay its debts generally as they become due; (h) modify the legal separateness provisions of the Pepco Holdings Operating Agreement; or (i) remove the unanimous consent requirement set forth above.

15. Each of the Pepco Holdings Utilities' bylaws were amended to require unanimous consent of the board of directors of such entity and approval of such entity's shareholder to (a)

commence any case, proceeding or other action on behalf of the company under any existing or future law of any jurisdiction relating to bankruptcy, insolvency, reorganization, or relief for debtors; (b) institute proceedings to have the company adjudicated as bankrupt or insolvent; (c) consent to or acquiesce in the institution of bankruptcy or insolvency proceedings against the company; (d) file a petition or consent to a petition seeking reorganization, arrangement, adjustment, winding-up, dissolution, composition, liquidation, or other relief on behalf of the company of its debts under any federal or state law relating to bankruptcy; (e) apply for, or consent to, or acquiesce in the appointment of, a receiver, liquidator, sequestrator, trustee or other officer with similar powers of such person with respect to the company; (f) make any assignment for the benefit of the company creditors; (g) admit in writing the company inability to pay its debts generally as they become due; or (h) adopt an amendment or repeal of the unanimous consent requirement set forth above.

16. Holdco will maintain arms-length relationships with each of its affiliates and observe all necessary, appropriate and customary company formalities in its dealings with its affiliates. Pepco Holdings and Pepco Holdings' subsidiaries will maintain arms-length relationships with Exelon and its affiliates, including Holdco.

17. At all times, Holdco will hold itself out as an entity separate from its affiliates, will conduct business in its own name through its duly authorized directors and officers and comply with all organizational formalities to maintain its separate existence and shall use commercially reasonable efforts to correct any known misunderstanding regarding its separate identity. Pepco Holdings and the Pepco Holdings Utilities will hold themselves out as separate entities from Exelon, EEDC and Holdco, conduct business in their own names (provided that Pepco Holdings and each of the Pepco Holdings Utilities may identify itself as an affiliate of Exelon on a basis consistent with Exelon's other utility subsidiaries).

18. Holdco shall maintain its own separate books, records, bank accounts and financial statements reflecting its separate assets and liabilities. Pepco Holdings and each of the Pepco Holdings Utilities will maintain separate books, accounts and financial statements reflecting its separate assets and liabilities.

19. Holdco shall comply with Generally Accepted Accounting Principles in the United States ("GAAP") in all material respects (subject, in the case of unaudited financial statements, to the absence of footnotes and to normal year-end audit adjustments) in all financial statements and reports required of it and issue such financial statements and reports separately from any financial statements or reports prepared for its affiliates; provided that such financial statements or reports may be consolidated with those of its affiliates if the separate existence of Holdco and its assets and liabilities are clearly noted therein.

20. Holdco shall account for and manage all of its liabilities separately from any other entity, and pay its own liabilities only out of its own funds.

21. Holdco shall neither guarantee nor become obligated for the debts of any other entity nor hold out its credit or assets as being available to satisfy the obligations of any other entity.

22. Each of the Pepco Holdings Utilities maintain separate debt and preferred stock, if any, so that none will be responsible for the debts or preferred stock of affiliated companies, and each will maintain its own corporate and debt credit rating as well as ratings for long-term debt and preferred stock, if any. Pepco Holdings and each of the Pepco Holdings Utilities will use reasonable efforts to maintain separate credit ratings for their publicly traded securities. Pepco Holdings does not have any outstanding, and will not issue any, long-term debt securities. Pepco Holdings and each of the Pepco Holdings Utilities will use reasonable efforts and prudence to preserve investment grade credit ratings.

23. Holdco will not commingle its funds or other assets with the funds or other assets of any other entity and shall not maintain any funds or other assets in such a manner that it will be costly or difficult to segregate, ascertain or identify its individual funds or other assets from those of its owners or any other person.

24. Pepco Holdings and each of the Pepco Holdings Utilities will maintain in its own name all assets and other interests in property used or useful in their respective business and will not transfer its ownership interest in any such property to Exelon or an Exelon affiliate (other than a Pepco Holdings subsidiary) without requisite approval of the applicable state or local regulatory commission and any approval required under the Federal Power Act; provided that the foregoing shall not limit the ability of Pepco Holdings to transfer to Exelon or Exelon affiliates any business or operations of Pepco Holdings or Pepco Holdings subsidiaries that are not regulated by state or local utility regulatory authorities.

25. Holdco shall ensure that its funds will not be transferred to its owners or affiliates except with the consent and authority of Holdco's board of directors.

26. Holdco shall ensure that title to all real and personal property acquired by it is acquired, held and conveyed in its name.

27. No entities other than Pepco Holdings and its subsidiaries, including the Pepco Holdings Utilities and PHI Service Company, will participate in the Pepco Holdings Utilities' money pool. The Pepco Holdings Utilities will not participate in any money pool operated by Exelon, and there will be no commingling of the Pepco Holdings money pool funds with funds of Exelon. Any deposits into or loans through the Pepco Holdings money pool by Pepco Holdings Utilities shall be on terms no less favorable than the depositor or lender could obtain through a short-term investment of similar funds with independent parties. Any borrowings from the Pepco Holdings money pool by one of the Pepco Holdings Utilities shall be on terms no less favorable

and cost effective than the Pepco Holdings Utility could obtain through short-term borrowings from (including sales of commercial paper to) independent parties.

28. Holdco will maintain a separate name from and will not use the trademarks, service marks or other intellectual property of Exelon, Pepco Holdings, or Pepco Holdings' subsidiaries. Pepco Holdings and the Pepco Holdings Utilities will each maintain a separate name from and will not use the trademarks, service marks or other intellectual property (i.e., identifying marks) of Exelon or its other affiliates, except that Pepco Holdings and each of the Pepco Holdings Utilities may identify itself as an affiliate of Exelon on a basis consistent with the practices of Exelon's other utility subsidiaries.

29. Any amendment to the organizational documents of Holdco that would remove or alter the voting or other Ring-Fencing Measures described above will require the unanimous vote of the board of directors of Holdco, including the independent director, and the affirmative consent of the holder of the Golden Share.

For purposes of this opinion, we have assumed that, following consummation of the Merger and the Separation, the Exelon Entities, Holdco, Pepco Holdings and the Pepco Holdings Utilities have complied and will comply with the Ring-Fencing Measures.

C. Holdco Operating Agreement

Holdco is a limited-purpose, limited liability company organized under the laws of the State of Delaware. EEDC and Member B are the sole members of Holdco, and collectively own 100% of the outstanding membership interests in Holdco.

EEDC, Member B and Holdco are party to the Holdco Operating Agreement, which sets forth the terms by which Holdco is operated, including the following (capitalized terms not otherwise defined in this Section I.C. having the meanings set forth in the Holdco Operating Agreement):

1. EEDC is the Class A Member holding 100% of the Class A Membership Units. The Class A Member is allocated all profits and losses and is entitled to all distributions from Holdco as specified in Sections 6.1 and 6.2 of the Holdco Operating Agreement.

2. Member B is the Class B Member holding 100% of the Class B Membership Units. Member B shall not be allocated any profits or losses and shall not be entitled to any distributions from Holdco as specified in Sections 6.1 and 6.2 of the Holdco Operating Agreement. The Class B Member shall not be required to make any capital contribution to Holdco at any time. The Holdco Operating Agreement further provides that the Class B Member is a Member for the sole and limited purpose of restricting the right of Holdco to take certain actions as set forth in Section 5.1(b) of the Holdco Operating Agreement, which relates to limitations on Holdco's activities,

including bankruptcy, insolvency and dissolution, among others, and Section 9.3 of the Holdco Operating Agreement, which relates to certain amendments to the Holdco Operating Agreement or its Certificate of Formation.

3. The permitted activities of Holdco are restricted by the Holdco Operating Agreement solely to (a) holding limited liability company interests of Pepco Holdings and (b) engaging in and performing any lawful act or activity and exercising any powers permitted to limited liability companies organized under the laws of the State of Delaware that are related or incidental to, and necessary, convenient or advisable for, the accomplishment of the purpose of holding the limited liability company interests of Pepco Holdings.

4. The Holdco Operating Agreement limits Holdco's performance of certain activities consistent with its special purpose nature; specifically, Holdco shall:

(a) not commingle its funds or other assets with the funds or other assets of any other Person, nor maintain any funds or other assets in such a manner that it will be costly or difficult to segregate, ascertain or identify its individual funds or other assets from those of its Members or any other Person;

(b) at all times hold itself out to the public and all other Persons as a legal entity separate from any other Person;

(c) conduct its business in its own name through its duly authorized Directors and Officers and comply with all organizational formalities to maintain its separate existence;

(d) not use the trademarks, service marks or other intellectual property of any of its Affiliates;

(e) maintain its own separate books, records, bank accounts and financial statements reflecting its separate assets and liabilities;

(f) maintain an arm's-length relationship with each of its Affiliates;

(g) maintain adequate capital in light of its contemplated business purpose, transactions and liabilities; provided, however, the foregoing shall not require the Members to make any additional capital contributions to Holdco;

(h) comply with GAAP in all material respects (subject, in the case of unaudited financial statements, to the absence of footnotes and to normal year-end audit adjustments) in all financial statements and reports required of it and issue such financial statements and reports separately from any financial statements or reports prepared for its Members and Affiliates; provided that such financial statements or reports may be consolidated with those of its Affiliates if the separate existence of Holdco and its assets and liabilities are clearly noted therein;

(i) account for and manage all of its liabilities separately from any other Person, and pay its own liabilities only out of its own funds;

(j) neither guarantee nor become obligated for the debts of any other Person nor hold out its credit or assets as being available to satisfy the obligations of any other Person;

(k) use commercially reasonable efforts to correct any known misunderstanding regarding its separate identity;

(l) ensure that title to all real and personal property acquired by it be acquired, held and conveyed in its name;

(m) observe all necessary, appropriate and customary company formalities in its dealings with its members and Affiliates;

(n) make all decisions with respect to its business and daily operations independently, although its Operating Directors and Officers making any particular decision may also be employees, officers, directors or managers of the Class A Member, its members or its Affiliates;

(o) ensure that its funds will not be transferred to the Class A Member or its Affiliates except with the consent and authority of the Board;

(p) not acquire, assume or guarantee obligations of any Affiliate;

(q) not pledge its assets for the benefit of any other Person or make loans to, or purchase or hold any indebtedness of, any other Person; and

(r) cause its Directors, Officers and its other representatives to act, in their reasonable discretion, at all times with respect to, consistently with, and in furtherance of, the foregoing.

5. Pursuant to Section 5.1(b) of the Holdco Operating Agreement, neither the Members nor the Board nor any Director nor any Officer nor any other Person shall be authorized or empowered, nor shall they permit Holdco, without the unanimous prior approval of the Board, including the Independent Director and the prior written consent of the Class B Member, to:

(a) commence any case, proceeding or other action on behalf of Holdco under any existing or future law of any jurisdiction relating to bankruptcy, insolvency, reorganization, or relief for debtors;

(b) institute proceedings to have Holdco adjudicated as bankrupt or insolvent;

(c) consent to or acquiesce in the institution of bankruptcy or insolvency proceedings against Holdco;

(d) file a petition or consent to a petition seeking reorganization, arrangement, adjustment, winding-up, dissolution, composition, liquidation, or other relief on behalf of Holdco of its debts under any federal or state law relating to bankruptcy;

(e) apply for, or consent to, or acquiesce in the appointment of, a receiver, liquidator, sequestrator, trustee or other officer with similar powers of such Person with respect to Holdco;

(f) make any assignment for the benefit of Holdco's creditors;

(g) admit in writing Holdco's inability to pay its debts generally as they become due;

(h) modify the provisions of the Holdco Operating Agreement which limit Holdco's activities; or

(i) remove the unanimous consent requirement of the Holdco Operating Agreement regarding (i) bankruptcy, insolvency, dissolution, reorganization, liquidation or any similar proceeding or (ii) the making of any assignments for the benefit of Holdco's creditors or modifications to the Holdco Operating Agreement which limit Holdco's activities thereunder.

D. Pepco Holdings Operating Agreement

The initial Members of Pepco Holdings were Exelon and EEDC. Immediately following the formation of Pepco Holdings, Exelon transferred its Interest to EEDC. Immediately following the formation of Pepco Holdings and the Transfer of Unregulated Businesses to EEDC as contemplated by Section 5.1.3(c) of the Pepco Holdings Operating Agreement, EEDC transferred its entire Interest as a Member to Holdco as an absolute conveyance with the intention of removing Pepco Holdings and the Pepco Holdings Utilities from the bankruptcy estate of Exelon and EEDC. Holdco was admitted as a Member as Successor to EEDC without any action by Pepco Holdings, the Members or the Board of Directors (capitalized terms not otherwise defined in this Section I.D. having the meanings set forth in the Pepco Holdings Operating Agreement).

Pursuant to Section X of the Pepco Holdings Operating Agreement, Pepco Holdings is required to comply with the following separateness provisions:

(a) Pepco Holdings shall hold itself out to the public and all other Persons as a legal entity separate from Exelon and its Affiliates and the Members and conduct business in accordance with the separateness provisions of the Pepco Holdings Operating Agreement.

(b) Pepco Holdings shall maintain its own separate books, records, accounts, and financial statements reflecting its separate assets and liabilities. Pepco Holdings shall maintain its financial statements separate from those of any other Person other than Pepco Holdings' consolidated Subsidiaries.

(c) Pepco Holdings will maintain in its own name all assets and other interests in property used or useful in its business and ensure that title to all real and personal property acquired by it is acquired, held and conveyed in its name. Pepco Holdings will not transfer its ownership interest in any such property to Exelon or an Affiliate of Exelon without approval, if required, of state or local utility regulatory authorities and any required approval under the Federal Power Act; provided that the foregoing shall not limit the ability of Pepco Holdings to transfer to Exelon, EEDC, the Members or other Affiliates of Exelon any business or operations of Pepco Holdings or its Subsidiaries that are not regulated by state or local utility regulatory authorities. Pepco Holdings shall not commingle its funds or other assets with the funds or other assets of any other Person, and not maintain any funds or other assets in such a manner that it will be costly or difficult to segregate, ascertain or identify its individual funds or other assets as separate from those of Affiliates, Members or any other Person.

(d) Pepco Holdings shall conduct its business in its own name through its duly authorized Directors, officers and agents and comply with all organizational formalities in its dealings with other Persons to maintain its separate existence. Pepco Holdings shall maintain a separate name from and will not use the trademarks, service marks or other intellectual property (i.e., identifying marks) of Exelon or other Affiliates of Exelon, except that Pepco Holdings may identify itself as an Affiliate of Exelon on a basis consistent with utility Subsidiaries of Exelon. Pepco Holdings shall use commercially reasonable efforts to correct any known misunderstanding regarding its separate identity. Pepco Holdings shall, conduct its dealings with other Persons (including the Members and Affiliates) on an arm's length, fair and reasonable basis.

(e) Pepco Holdings shall not assume liability for the debts of Exelon, the Members, or any other Affiliate of Pepco Holdings other than a Company Subsidiary. Pepco Holdings shall not guarantee the debt or credit instruments of Exelon, the Members, or any Affiliate of the Company other than a Company Subsidiary. Pepco Holdings will use reasonable efforts and prudence to preserve investment grade credit ratings. Pepco Holdings shall account for and manage all of its liabilities separately from any other Person and pay its obligations and liabilities out of its own funds. Pepco Holdings shall not hold out its credit as being available to satisfy the obligations or liabilities of any other Person other than a Company Subsidiary, except for obligations or liabilities relating to assets transferred to Pepco Holdings or a Company Subsidiary from any other Person. Pepco Holdings shall maintain adequate capital in light of its contemplated business purpose, transactions and liabilities; provided, however, the foregoing shall not require the Members to make any additional capital contributions to Pepco Holdings.

In addition, pursuant to Section 5.2.9 of the Pepco Holdings Operating Agreement, the unanimous prior approval of Pepco Holdings Board of Directors is required to: (a) commence any case, proceeding or other action on behalf of Pepco Holdings under any existing or future law of any jurisdiction relating to bankruptcy, insolvency, reorganization, or relief for debtors; (b) institute proceedings to have Pepco Holdings adjudicated as bankrupt or insolvent; (c) consent to or acquiesce in the institution of bankruptcy or insolvency proceedings against Pepco Holdings; (d) file a petition or consent to a petition seeking reorganization, arrangement, adjustment, winding-up, dissolution, composition, liquidation, or other relief on behalf of Pepco Holdings of its debts under any federal or state law relating to bankruptcy; (e) apply for, or consent to, or acquiesce in the appointment of, a receiver, liquidator, sequestrator, trustee or other officer with similar powers of such Person with respect to Pepco Holdings; (f) make any assignment for the benefit of Pepco Holdings' creditors; (g) admit in writing the Pepco Holdings' inability to pay its debts generally as they become due; (h) modify the provisions of Section X of the Pepco Holdings Operating Agreement; or (i) remove the unanimous consent requirement set forth above.

E. Intercompany Relationship Among the Exelon Entities, Holdco, Pepco Holdings and the Pepco Holdings Utilities

We have assumed that the following statements are true in all material respects on the date hereof and will remain true in all material respects at all other times relevant to this opinion:

1. Holdco has acted and will act in accordance with the requirements of the Holdco Operating Agreement.

2. Pepco Holdings has acted and will act in accordance with the requirements of the Pepco Holdings Operating Agreement.

3. The Exelon Entities, Holdco, Pepco Holdings and the Pepco Holdings Utilities will comply with the Ring-Fencing Measures.

4. EEDC may, from time to time, contribute assets to Holdco, which contributions will be properly reflected in the books and records of Holdco. Any capital contributions by EEDC to Holdco will be, in all instances, made in good faith and without actual intent to hinder, delay, or defraud any creditors. If EEDC elects to make a capital contribution to Holdco, the contribution will increase the value of EEDC's equity interest in Holdco. Any capital contribution, if made, will be properly reflected in the books and records of Holdco and EEDC and will be made in compliance with the Holdco Operating Agreement and applicable law. However, EEDC is under no obligation to make such contributions.

5. All corporate formalities and actions will be observed and performed in connection with any transfer of assets, including transfers between Holdco and the Exelon Entities or between Pepco Holdings and/or any of the Pepco Holdings Utilities and Holdco.

6. On the date hereof, Exelon has substantial going concern value, and the management of Exelon reasonably believes that Exelon is: (a) adequately capitalized to conduct its business and affairs as a going concern and to meet its financial obligations without the need for capital contributions, (b) solvent, (c) able to pay its debts as they come due, and (d) as a result, currently able to stand alone as an independent entity.

7. On the date hereof, EEDC has substantial going concern value, and the management of EEDC reasonably believes that EEDC is: (a) adequately capitalized to conduct its business and affairs as a going concern and to meet its financial obligations without the need for capital contributions, (b) solvent, (c) able to pay its debts as they come due, and (d) as a result, currently able to stand alone as an independent entity

8. On the date hereof, Holdco has substantial going concern value, and the management of Holdco reasonably believes that Holdco is: (a) adequately capitalized to conduct its business and affairs as a going concern and to meet its financial obligations without the need for capital contributions, (b) solvent, (c) able to pay its debts as they come due, and (d) as a result, currently able to stand alone as an independent entity.

9. On the date hereof, Pepco Holdings has substantial going concern value, and the management of Pepco Holdings reasonably believes that Pepco Holdings is: (a) adequately

capitalized to conduct its business and affairs as a going concern and to meet its financial obligations without the need for capital contributions, (b) solvent, (c) able to pay its debts as they come due, and (d) as a result, currently able to stand alone as an independent entity.

10. On the date hereof, ACE has substantial going concern value, and the management of ACE reasonably believes that ACE is: (a) adequately capitalized to conduct its business and affairs as a going concern and to meet its financial obligations without the need for capital contributions, (b) solvent, (c) able to pay its debts as they come due, and (d) as a result, currently able to stand alone as an independent entity.

11. On the date hereof, Delmarva has substantial going concern value, and the management of Delmarva reasonably believes that Delmarva is: (a) adequately capitalized to conduct its business and affairs as a going concern and to meet its financial obligations without the need for capital contributions, (b) solvent, (c) able to pay its debts as they come due, and (d) as a result, currently able to stand alone as an independent entity.

12. On the date hereof, Pepco has substantial going concern value, and the management of Pepco reasonably believes that Pepco is: (a) adequately capitalized to conduct its business and affairs as a going concern and to meet its financial obligations without the need for capital contributions, (b) solvent, (c) able to pay its debts as they come due, and (d) as a result, currently able to stand alone as an independent entity.

13. The Exelon Entities, Holdco, Pepco Holdings and the Pepco Holdings Utilities each has taken and will take such other actions as are reasonably necessary on its part to ensure that facts and assumptions set forth in this opinion remain true and correct in all material respects at all times.

14. Exelon, Pepco Holdings and the Pepco Holdings Utilities have disclosed and will continue to disclose the existence of Holdco and the implementation of the Ring-Fencing Measures in their respective periodic and other reports under the Securities Exchange Act of 1934, which reports will be publicly available (the "Holdco Disclosure Reports").

II. DISCUSSION OF SUBSTANTIVE CONSOLIDATION

A. Discussion of Case Law

Substantive consolidation is a judicially created doctrine arising from the general equity powers granted to bankruptcy courts.[1] It has generally been recognized that no specific provision

[1] F.D.I.C. v. Colonial Realty Co., 966 F.2d 57, 59 (2d Cir. 1992); Eastgroup Properties v. Southern Motel Assocs., 935 F.2d 245, 248 (11th Cir. 1991); In re Auto-Train Corp., Inc., 810 F.2d 270, 276 (D.C. Cir. 1987); In re Continental Vending Mach. Corp., 517 F.2d 997, 1000 (2d Cir. 1975), cert. denied, 424 U.S. 913

of the Bankruptcy Code expressly authorizes a court to order substantive consolidation and that such authority is derived from Section 105(a) of the Bankruptcy Code, which provides that: "The court may issue any order, process, or judgment that is necessary or appropriate to carry out the provisions of the Bankruptcy Code."[2] One case, however, suggests that Section 1123(a)(5) of the Bankruptcy Code authorizes substantive consolidation in the context of a plan of reorganization.[3]

Under the doctrine of substantive consolidation, a bankruptcy court may, if appropriate circumstances are determined to exist, consolidate the assets and liabilities of different entities by merging the assets and liabilities of the entities and treating the related entities as a consolidated entity for purposes of the bankruptcy proceedings. "[T]he intercompany claims of the debtor companies are eliminated, the assets of all debtors are treated as common assets and claims of outside creditors against any of the debtors are treated as against the common fund . . . ."[4]

(1976); In re Affiliated Foods, Inc., 249 B.R. 770 (Bankr. W.D. Mo. 2000); In re Drexel Burnham Lambert Group, Inc., 138 B.R. 723 (Bankr. S.D.N.Y. 1992); In re Alico Mining, Inc., 278 B.R. 586, 588 (Bankr. M.D. Fl. 2002); In re Central European Industrial Development Co. LLC, 288 B.R. 572, 576 (Bankr. N.D. Cal. 2003); In re American Homepatient, Inc., 298 B.R. 152 (Bankr. M.D. Tenn. 2003), aff'd, 420 F.3d 559 (6th Cir. 2005).

2 2 Collier on Bankruptcy ¶ 105.09[1][b], at 105-90-91 (Alan N. Resnick & Henry J. Sommer eds., 16th rev. ed 2010). See generally id. at ¶ 105.09. at 105-90-107; Second Interim Report of Neal Batson, Court-Appointed Examiner, dated January 21, 2003, filed in connection with In re Enron Corp., Case No. 01-16034 (AJG) Jointly Administered (Bankr. S.D.N.Y.) (the "Second Batson Report") at 32-33.

3 See In re Stone & Webster, Inc., 286 B.R. 532, 541-543 (Bankr. D.Del. 2002).

4 Chemical Bank New York Trust Co. v. Kheel, 369 F.2d 845, 847 (2d Cir. 1966). See Eastgroup Properties, 935 F.2d at 248 ("[Substantive consolidation] involves the pooling of assets and liabilities of two or more related entities; the liabilities of the entities involved are then satisfied from the common pool of assets created by consolidation."); Colonial Realty, 966 F.2d at 58-59; In re Augie/Restivo Baking Co., 860 F.2d 515, 518 (2d Cir. 1988); In re Snider Bros., Inc., 18 B.R. 230, 234 (Bankr. D. Mass. 1982) (consolidation enables the court to disregard corporate entities in order to reach assets for the satisfaction of creditors of a related corporation); In re GC Companies, Inc., 274 B.R. 663, 672 (Bankr. D.Del. 2002) rev'd on other grounds, 298 B.R. 226 (D. Del. 2003). Substantive consolidation is not to be confused with joint administration (also known as procedural consolidation), "in which inter alia, all docketing and noticing is done in one case file for more than one related case, but the estates and creditor bodies are not merged." In re Cooper, 147 B.R. 678, 682 (Bankr D. N.J. 1992).

Certain courts have held that they can consolidate estates as to certain claims (e.g., unsecured claims) even if it is not consolidating as to all claims. See, e.g., Cooper, 147 B.R. at 682; accord In re Parkway Calabasas Ltd., 89 B.R. 832, 837 (Bankr. C.D. Cal. 1988) (noting that to protect creditors, court may qualify the consolidation or only consolidate certain claims—unsecured rather than secured), aff'd, 949 F.2d 1058 (9th Cir. 1991); see In re Gulfco Inv. Corp., 593 F.2d 921, 927 (10th Cir. 1979) (substantive consolidation cannot reduce secured creditors to the status of unsecured creditors absent circumstances like fraud); see also

Given that the power to order substantive consolidation derives from the equity jurisdiction of the bankruptcy courts, the issue is determined on a case-by-case basis and the decisions reflect the courts' analysis of the particular factual circumstances presented.[5] A court's inquiry requires an examination, inter alia, of the structures of the entities proposed to be consolidated, their intercorporate relationships, and their relationships with their respective creditors and other third-parties. Because the doctrine of substantive consolidation is an equitable one, the court often will also examine, inter alia, the impact upon each entity if consolidation were to be ordered, and whether such parties would be unfairly prejudiced or treated more equitably by substantive consolidation.[6]

The case law indicates a general recognition that substantive consolidation is an extraordinary remedy vitally affecting substantive rights, which, due to the potential inequities caused by the fact that consolidation almost invariably redistributes wealth among the creditors of consolidated entities, should only rarely be granted.[7] Similarly, because the disregard of separate existence is not generally favored, a presumption arises against substantive consolidation and the

Continental Vending Mach., 517 F.2d at 1000-02, wherein the court consolidated the cases for purposes of ascertaining the rights of unsecured creditors while leaving the position of secured creditors intact.

5 See 2 Collier on Bankruptcy ¶ 105.09[2], at 105-93 (Alan N. Resnick & Henry J. Sommer eds., 16th rev. ed. 2010) (stating that substantive consolidation cases are to a great degree sui generis).

6 See Augie/Restivo, 860 F.2d at 518; In re Central European Industrial Development Co. LLC, 288 B.R. at 576 (the primary purpose of substantive consolidation is to "insure the equitable treatment of all creditors").

7 In re Amco Ins., 444 F.3d 690, 697 (5th Cir. 2006) (noting in dicta that jurisdictions that allow substantive consolidation emphasize that it should be used 'sparingly'), cert. denied, 127 S. Ct. 389 (2006); In re Owens Corning, 419 F.3d 195, 208-9 (3d Cir. 2005) ("[T]here appears nearly unanimous consensus that [substantive consolidation] . . . is a remedy to be used 'sparingly'"); Auto-Train, 810 F.2d at 276; Augie/Restivo, 860 F.2d at 518; In re New Century TRS Holdings, Inc., 407 B.R. 576, 591 (D.Del. 2009) ("Because substantive consolidation is 'extreme' . . . and 'imprecise,' it works 'rough justice' and is to be used sparingly."); In re Source Enterprises, Inc., 392 B.R. 541, 552 (S.D.N.Y. 2008) (The sole purpose of substantive consolidation is "'to ensure the equitable treatment of all creditors and it is to be used 'sparingly.'"); In re American Camshaft Specialties, Inc., 410 B.R. 765, 786 (Bankr. E.D. Mich. 2009) ("The reason [that courts are reluctant to order substantive consolidation] is that "the doctrine authorizes a court to look past the limited liability that is a hallmark of corporate law in the United States and the legal separateness that it provides for."); Snider Bros., 18 B.R. at 234 ("substantive consolidation, in almost all instances, threatens to prejudice the rights of creditors. . . . This is so because separate debtors will almost always have different ratios of assets to liabilities."); Kheel, 369 F.2d at 847 ("The power to consolidate should be used sparingly because of the possibility of unfair treatment of creditors of a corporate debtor who have dealt solely with that debtor without knowledge of its interrelationship with others."); see also Eastgroup Properties, 935 F.2d at 248; In re World Access, Inc., 301 B.R. 217, 272 (Bankr. N.D. Ill. 2003).

party seeking to substantively consolidate bears the burden of establishing the necessity for it. Thus, substantive consolidation is the exception rather than the rule.[8]

The initial cases ordering substantive consolidation generally involved fact patterns where it was alleged that one or more entities were "mere instrumentalities" or "alter egos" of one another. These cases often involved allegations of the use of an entity to hinder, delay or defraud creditors and involved state law concepts similar to the doctrine of piercing the corporate veil.[9] Subsequent cases generally departed from utilizing these state law concepts in favor of a federal body of law. Some courts have in these cases ordered substantive consolidation where, among other things, the proponents have demonstrated either (i) a harm to be avoided or (ii) a benefit to be effected generally which, under the circumstances and considering whether the rights of third-parties would be unduly prejudiced thereby, it is equitable to effect.[10] In addition, courts

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[8] See e.g., Auto-Train Corp., Inc., 810 F.2d at 276; Continental Vending Mach. Corp., 517 F.2d at 1001; Kheel, 369 F.2d at 847 (it should be the "rare case" where substantive consolidation is granted); In re DRW Property Co., 54 B.R. 489, 494 (Bankr. N.D. Tex. 1985) (courts should grant substantive consolidation sparingly because of the possibility of unfair treatment of some creditors); Second Batson Report at 33-34 (summarizing several Second Circuit cases holding that substantive consolidation "should be used sparingly" and "[t]he party seeking substantive consolidation has the burden of proof").

[9] See, e.g., Stone v. Eacho, 127 F.2d 284 (4th Cir. 1942), cert. denied, 317 U.S. 635 (1942); Fish v. East, 114 F.2d 177 (10th Cir. 1940); Maule Industries Inc. v. Cerstel, 232 F.2d 294 (5th Cir. 1956). The court in Fish, 114 F.2d at 191, set forth an often-quoted list of factors to be considered in determining whether one entity is a "mere instrumentality" of another: the parent corporation owns all or a majority of the capital stock of the subsidiary; the parent and subsidiary corporations have common directors or officers; the parent corporation finances the subsidiary; the parent corporation subscribes to all the capital stock of the subsidiary or otherwise causes its incorporation; the subsidiary has grossly inadequate capital; the parent corporation pays the salaries or expenses or losses of the subsidiary; the subsidiary has substantially no business except with the parent corporation or no assets except those conveyed to it by the parent corporation; in the papers of the parent corporation, and in the statements of its officers, "the subsidiary" is referred to as a mere instrumentality or as a department or division; the directors or executives of the subsidiary do not act independently in the interest of the subsidiary, but take direction from the parent corporation; and the formal legal requirements of the subsidiary as a separate and independent corporation are not observed. For more recent cases involving these concepts, see In re I.R.C.C., Inc., 105 B.R. 237, 242 (Bankr. S.D.N.Y. 1989); Cooper, 147 B.R. at 683; In re Moran Pipe & Supply Co., 130 B.R. 588, 591 (Bankr. E.D. Okla. 1991); In re Mortgage Inv. Co. of El Paso, Tex., 111 B.R. 604, 610 (Bankr. W.D. Tex. 1990).

[10] Eastgroup Properties, 935 F.2d at 249 ("[T]he basic criterion by which to evaluate a proposed substantive consolidation is whether 'the economic prejudice of continued debtor separateness' outweighs 'the economic prejudice of consolidation.'"); In re Giller, 962 F.2d 796, 799 (8th Cir. 1992) (factors to consider include whether the benefits of consolidation outweigh the harm to creditors, and the prejudice resulting from not consolidating the debtors); In re Hemingway Transp., Inc., 954 F.2d 1, 12 (1st Cir. 1992) ("[T]he party requesting substantive consolidation must satisfy the bankruptcy court that, on balance, consolidation will foster a net benefit among all holders of unsecured claims."), cert. denied, 510 U.S. 914 (1993); In re Central European Industrial Development Co. LLC, 288 B.R. at 576. In order to properly apply this balancing of interests "a court must conduct a searching inquiry to ensure that consolidation yields benefits offsetting the

have ordered substantive consolidation where interrelationships among entities have become hopelessly entangled, and there would be great difficulty and expense in separating the assets, liabilities, and businesses of the entities so that separate administration would not be practicable, i.e., "the time and expense necessary even to attempt to unscramble [the intercompany relationships and transactions] are so substantial as to threaten the realization of any net assets for all the creditors. . . ."[11] One Second Circuit decision summarizes the key factors as (i) whether creditors dealt with the entities as a single economic unit and did not rely on their separate identity in extending credit or (ii) whether the affairs of the debtors are so entangled that consolidation will benefit all creditors.[12] The Third Circuit adopted a somewhat similar test holding that:

> In our Court what must be proven (absent consent) concerning the entities for whom substantive consolidation is sought is that (i) prepetition they disregarded

harm it inflicts on objecting parties." Auto-Train, 810 F.2d at 276; Snider Bros., 18 B.R. at 238; Eastgroup Properties, 935 F.2d at 249; Soviero v. Franklin National Bank of Long Island, 328 F.2d 446, 447-48 (2d Cir. 1964); In re Amereco Envtl. Servs., 125 B.R. 566, 568 (Bankr. W.D. Mo. 1991); accord In re Vecco Constr. Indus., 4 B.R. 407 (Bankr. E.D. Va. 1980) (creditors did not object); In re F.A. Potts & Co., 23 B.R. 569 (Bankr. E.D. Pa. 1982) (objecting creditors failed to establish undue prejudice); In re Stevenson, 153 B.R. 52 (Bankr. D. Idaho 1993) (main requirement for substantive consolidation is that no creditor's or interested party's rights be prejudiced); In re Alico Mining Co., 278 B.R. at 589 (proponent must show substantial identity between the entities to be consolidated and that consolidation is necessary to avoid some harm or to realize some benefit). One lower court has held that substantive consolidation can be effected, in the absence of creditor objection, where the debtors functioned as a consolidated entity and had multiple inter-debtor guarantees and debts. In re Standard Brands Paint Company, 154 B.R. 563, 571-72 (Bankr. C.D. Cal. 1993).

11 Kheel, 369 F.2d at 847. In Kheel, several debtor corporations were owned and controlled by the same individual and operated as a single unit without regard to corporate formalities observed by independent corporations. Funds were transferred and loans were made between corporations without proper record keeping, debts were incurred to pay the obligations of related corporations and the corporations collected funds and paid expenses for their common owner. The court ordered consolidation based upon the practical impossibility of sorting out the debtor's records to determine intercorporate claims and their separate assets and liabilities, and because even if such an effort were undertaken there would be no assurance that a fair reflection of the financial condition of each individual debtor could be obtained. See also Continental Vending Mach., 517 F.2d at 1001 (the inequities among creditors caused by substantive consolidation "must be heavily outweighed by practical considerations such as the accounting difficulties (and expense) which may occur where the interrelationships of the corporate group are highly complex, or perhaps untraceable"); Augie/Restivo, 860 F.2d at 519 (notwithstanding entanglement of records and business affairs, consolidation "should be used only after it has been determined that all creditors will benefit because untangling is either impossible or so costly as to consume the assets"). See also Nesbit v. Gears Unlimited, Inc., 347 F.3d 72, 87 fn. 7 (3d Cir. 2003), cert. denied, 541 U.S. 959 (2004) (summarizing the various tests used by the different Circuit Courts of Appeals); In re Homepatient, Inc., 298 B.R. at 165-66.

12 Augie/Restivo, 860 F.2d at 518. See also In re Bonham, 229 F.3d 750 (9th Cir. 2000) (adopting Augie/Restivo test); In re Brentwood Golf Club, L.L.C., 329 B.R. 239 (E.D. Mich. 2005) (applying Augie/Restivo test).

> separateness so significantly their creditors relied on the breakdown of entity borders and treated them as one legal entity, or (ii) postpetition their assets and liabilities are so scrambled that separating them is prohibitive and hurts all creditors.

In re Owens Corning, 419 F.3d at 211 (citations omitted).[13]

Courts have also ordered substantive consolidation where consolidation would enhance the debtor's chances of successful reorganization.[14] Arguably, certain of these cases reflect "the courts' recognition of the increasingly widespread existence in the business world of parent and subsidiary corporations with interrelated corporate structures and functions"[15] and suggest that, in the absence of harm or prejudice to any particular group, a court would be less concerned with

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13 See also In re American Camshaft Specialties, Inc. 410 BR at 787 (Bankruptcy Court in Michigan adopts Owens Corning analysis in the absence of a decision on point by the Sixth Circuit).

14 In re Manzey Land & Cattle Co., 17 B.R. 332, 338 (Bankr. D.S.D. 1982) ("One of the policies behind the enactment of Chapter 11 is to give a debtor one meaningful and reasonable chance to rehabilitate. This Court finds substantive consolidation in this case furthers that intent of Congress."); F.A. Potts & Co., 23 B.R. at 573 ("[S]ubstantive consolidation is necessary to facilitate the filing of a comprehensive and consolidated plan of reorganization."); In re Munford Inc., 115 B.R. 390, 396 (Bankr. N.D. Ga. 1990) ("impact of consolidation on the chances of successful reorganization is another well used criterion to justify substantive consolidation").

15 F.A. Potts & Co., 23 B.R. at 571; see also Eastgroup Properties, 935 F.2d at 248-249 (noting a "modern or liberal" trend toward allowing substantive consolidation in "recognition of the widespread use of interrelated corporate structures by subsidiary corporations operating under a parent entity's corporate umbrella. . . ."); Vecco Construction, 4 B.R. at 407; In re Interstate Stores, Inc., 1 B.R. 755 (Bankr. S.D.N.Y. 1980). It has been suggested that such recognition of interrelated corporate structures expresses a view known as "enterprise law": the application of legal principles based upon a finding that related debtors are conducting an economically integrated business as consistent parts of a single enterprise, notwithstanding formal organization of the components as separate legal entities. See Phillip I. Blumberg, The Law of Corporate Groups: Procedural Problems of Parent & Subsidiary Corporations, §§ 1.03, 10.10.1 (1985). That commentator has also stated that:

> Although the [Kheel] case noted that consolidation was to be used sparingly and this theme has been echoed on a number of occasions since, the reality is plain: The courts are increasingly ready to order consolidation for economically integrated debtors in a corporate group when it will implement the administration of the estate.

Id. at §10.11.7. But see In re Owens Corning, 419 F.3d at 209 n. 15 ("[W]e disagree with the assertion of a 'liberal trend' toward use of substantive consolidation – e.g. Eastgroup . . ."); In re World Access, Inc., 301 B.R. at 272 fn. 57 ("Although certain courts have observed a 'modern' trend toward more 'liberal' application of the doctrine, this Court is skeptical of the liberal approach.") (citations omitted).

traditional concepts. For instance, under a test followed by a number of courts, including the District of Columbia Circuit and the Eleventh Circuit (the "Balancing Test"), the proponent of substantive consolidation must show: (1) a substantial identity between the entities to be consolidated; and (2) that consolidation is necessary to avoid some harm or to realize some benefit.[16] If such showing is made, then, if a creditor objects and demonstrates that it relied on the separate credit of one of the entities and that it will be prejudiced by the consolidation, the court may order consolidation only if it determines that the benefits of consolidation "heavily" outweigh the harm.[17] Thus, before permitting substantive consolidation, the courts in these cases have still emphasized the absence of any harm or prejudice to any particular group, or have concluded, after considering the equities, that any harm or prejudice is outweighed by the benefits of substantive consolidation.[18]

With respect to the first two prongs of the Balancing Test, certain courts have sometimes used a checklist of factors. The court in Vecco Construction, 4 B.R. at 410, enumerated certain of the most widely cited criteria for determining whether consolidation is prima facia appropriate:

1. The commingling of assets and business functions.

2. The degree of difficulty in segregating and ascertaining individual assets and liabilities.

3. The existence of parent and intercorporate guarantees of loans.

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16 See, e.g., Auto-Train, 810 F.2d at 276; Eastgroup Property, 935 F.2d at 249 (adopting Balancing Test); see also Reider v. FDIC (In re Reider), 31 F.3d 1102, 1108-09 (11th Cir. 1994) (adopting Balancing Test as modified in the context of debtor spouses); In re Giller, 962 F.2d at 796 (adopting similar test considering: (1) the necessity of consolidation due to the interrelationship among the debtors; (2) whether the benefits of consolidation outweigh the harm to creditors; and (3) prejudice resulting from not consolidating the debtors); In re Affiliated Foods, Inc., 249 B.R. 770 (Bankr. W.D. Mo. 2000) (adopting In re Giller test). But see In re Owens Corning, 419 F.3d at 210 ("[W]e disagree that '[i]f a creditor makes [a showing of reliance on separateness], the court may order consolidation . . . if it determines that the demonstrated benefits of consolidation 'heavily' outweigh the harm).'"

17 Id.

18 See also Manzey Land & Cattle Co., 17 B.R. at 338 (no prejudice); F.A. Potts & Co., 23 B.R. at 574 (no prejudice); Munford, 115 B.R. at 395-96 (on a motion to dismiss a substantive consolidation complaint, the court indicated that consolidation would not prejudice creditors); In re Nite Lite Inns, 17 B.R. 367, 371 (Bankr. S.D. Cal. 1982) (no prejudice); In re Murray Industries Inc., 119 B.R. 820, 832 (Bankr. M.D. Fla. 1990) (the court concluded, after consideration of the relevant equities and noting the support of the official creditors' committee for substantive consolidation, that the benefits to creditors from substantive consolidation outweighed the prejudice to an equity holder and a creditor who was an insider).

4. The transfer of assets without observance of corporate formalities.

5. The presence or absence of consolidated financial statements.

6. The unity of interests and ownership between the various corporate entities.

7. The profitability of consolidating at a single physical location.

In addition to the Vecco criteria, the court in Eastgroup included the following additional factors in applying the test described above:

1. The entities having common officers or directors.

2. The subsidiary being grossly undercapitalized.

3. The subsidiary transacting business solely with the parent.

4. Both entities disregarding the legal existence of the subsidiary as a separate organization.

See Eastgroup, 935 F.2d at 250. Because decisions regarding substantive consolidation are made on a case-by-case basis by a court of equity, there is no certainty as to the factors on which a court will focus in a particular case. However, the existence of several of the factors listed above should not, by themselves, result in the application of the substantive consolidation doctrine. See In re Creditors Serv. Corp., 195 B.R. 680, 690 (Bankr. S.D. Ohio 1996)(the factors merely provide the framework to assist a court's inquiry).[19]

The United States Court of Appeals for the Second Circuit by contrast has ruled that merely furthering the reorganization effort is not, in the absence of the more traditional factors, enough to warrant substantive consolidation.[20] The Second Circuit stated:

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19 See, also, Eastgroup Properties, 935 F.2d at 250; Snider Bros, 18 B.R. at 234; see also In re World Access, Inc., 301 B.R. at 277 (holding that proponents of substantive consolidation did not make a prima facie case for consolidation even though certain of the Vecco Construction factors were met where other "more important factors" were not met, such as commingling of assets, poor record keeping causing difficulty in segregating assets and transfers made without observance of corporate formalities).

20 Unlike the cases cited supra note 32 in which no prejudice was found to exist, the Second Circuit in Augie/Restivo found that consolidation would unfairly prejudice the principal creditor of one of the debtors. Augie/Restivo, 860 F.2d at 520.

> [W]e do not believe that a proposed reorganization plan alone can justify substantive consolidation. Where, as in the instant case, creditors such as Union and MHTC knowingly made loans to separate entities and no irremediable commingling of assets has occurred, a creditor cannot be made to sacrifice the priority of its claims against its debtor by fiat based on the bankruptcy court's speculation that it knows the creditor's interests better than does the creditor itself.[21]

In a well-reasoned case, the Third Circuit in Owens Corning summarized the case law as follows:

> Ultimately most courts slipstreamed behind two rationales--those of the Second Circuit in Augie/Restivo and the D.C. Circuit in Auto-Train. The former found that the competing "considerations are merely variants on two critical factors: (i) whether creditors dealt with the entities as a single economic unit and did not rely on their separate identity in extending credit . . . or (ii) whether the affairs of the debtors are so entangled that consolidation will benefit all creditors . . . ." In re Augie/Restivo, 860 F.2d at 518 (internal quotation marks and citations omitted). Auto-Train touched many of the same analytical bases as the prior Second Circuit cases, but in the end chose as its over-arching test the "substantial identity" of the entities and made allowance for consolidation in spite of creditor reliance on separateness when "the demonstrated benefits of consolidation 'heavily' outweigh the harm." In re Auto-Train, 810 F.2d at 276 (citation omitted).[22]

The court then went on to criticize the Balancing Test as set forth in the Auto-Train decision by stating as follows:

> To us [the Auto-Train test] fails to capture completely the few times substantive consolidation may be considered and then, when it does hit one chord, it allows a threshold not sufficiently egre-gious and too imprecise for easy measure. For example, we disagree that "if a creditor makes [a showing of reliance on separateness], the court

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[21] Augie/Restivo, 860 F.2d at 520; accord, In re Owens Corning, 419 F.3d at 203.

[22] 419 F.3d at 207-208.

> may order consolidation . . . if it determines that the demonstrated benefits of consolidation 'heavily' outweigh the harm." If an objecting creditor relied on the separateness of the entities, consolidation cannot be justified vis-à-vis the claims of that creditor.[23]

We note that certain courts have not permitted (or have been very hesitant to permit) substantive consolidation where one party is a debtor and the other is not a debtor in a bankruptcy case, and so if Exelon or EEDC were a debtor in a bankruptcy case, but Holdco was not, or if Exelon, EEDC or Holdco was a debtor in a bankruptcy case, but Pepco Holdings or any of the Pepco Holdings Utilities was not, a proponent of substantive consolidation may face an additional hurdle.[24]

B. Application of Case Law Principles

As is evident from the discussion above, there is no single dispositive factor or set of factors applied consistently in substantive consolidation cases. Indeed, the courts have developed several different analytical frameworks. Under any of those frameworks, however, a bankruptcy court of competent jurisdiction should not apply the doctrine of substantive consolidation to consolidate (a) the assets and liabilities of Holdco with the assets and liabilities of Exelon and/or EEDC or (b) the assets and liabilities of Pepco Holdings or the Pepco Holdings Utilities with the assets and liabilities of Exelon, EEDC and/or Holdco, as the case may be.

The application of the doctrine of substantive consolidation is extremely fact-intensive and relates to facts not only as they exist now, but also as they may exist in the future. Accordingly, case law is only a general guide in attempting to anticipate what circumstances merit its

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[23] Id. at 210.

[24] 2 Collier on Bankruptcy, ¶ 105.09[1][c] at 105-92 (courts divided on whether to permit consolidation of a debtor with a nondebtor, but most courts permit such consolidation); see also In re Lease-A-Fleet, Inc., 141 B.R. 869, 872 (Bankr. E.D. Pa. 1992) ("[C]aution must be multiplied exponentially in a situation where a consolidation of a debtor's case with a non-debtor is attempted, by a single party which . . . is a creditor of the debtor only and whose efforts are not joined by any other interested parties."); In re Alpha & Omega Realty, Inc., 36 B.R. 416 (Bankr. D. Idaho 1984). Cf. Chauncey H. Levy, Joint Administration and Consolidation, 85 Comm. L.J. 538, 589 & nn.9-10 (1980). (Certain courts have held that substantive consolidation can be used with similar effect to extend the debtor's bankruptcy proceeding to include in the debtor's estate the assets of a related entity which is not a debtor in a case under the Bankruptcy Code); Munford, 115 B.R. 398 (Substantive consolidation "is recognized as an alternative means to bring a non-debtor's assets into a debtor's estate."); In re Owens Corning, 419 F.3d at 208 n. 13 (agreeing that substantive consolidation can be used to consolidate a non-debtor with a debtor); 2 Collier on Bankruptcy, ¶105.09[1][c] (15th ed. rev. 2005) ("The courts are divided on whether they may order consolidation of a debtor with a nondebtor.").

application. Thus, the question whether, and in what circumstances, a court would order substantive consolidation cannot be definitively answered in the abstract, but must take into account the actual facts and circumstances of the operation and relations of those entities over time. Accordingly, any opinion on substantive consolidation, including this opinion letter, is particularly dependent on the factual assumptions, such as those made in Part I of this opinion letter.[25]

1. **Substantial Identity**

Based upon the facts and assumptions contained herein which we have assumed are and will continue in the future to be true, we believe that it would be very difficult for a party in interest in a federal bankruptcy proceeding under the Bankruptcy Code to successfully claim that recognition of the Exelon Entities as separate from Holdco or recognition of Pepco Holdings and the Pepco Holdings Utilities as separate from the Exelon Entities and Holdco would be inequitable, or result in a fraud or injustice on creditors, or that Holdco, Pepco Holdings or the Pepco Holdings Utilities were a "mere instrumentality" or "alter ego" of the Exelon Entities or Holdco, as applicable.[26]

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25 In this regard, we note that certain of the facts cited in the bankruptcy court's opinion in In re Buckhead Am. Corp., Nos. 91-978 to 91-986 (Bankr. D. Del. August 13, 1992) as the basis for the substantive consolidation of the debtors named therein (such as commingling of bank accounts, payment of debtors' expenses from one joint account and entangled interrelationships) are different than those assumed herein and also appear to be different from the facts which, we understand, provided the basis for a legal opinion delivered prior to the commencement of the bankruptcy case that certain of such debtors would not be substantively consolidated.

26 We note in this respect that, absent findings of fraud or bad faith, courts have held that a corporation is entitled to a presumption of separateness from an affiliated corporation. Crown Cent. Petroleum Corp. v. Cosmopolitan Shipping Co., 602 F.2d 474, 476 (2d Cir. 1979); Pauley Petroleum, Inc. v. Continental Oil Co., 231 A.2d 450, 452 (Del. Ch. 1967), aff'd 239 A.2d 629 (Del. 1968). The Supreme Court has specifically ruled that "legitimate good faith business transactions [between affiliated corporations], neither in design or effect producing injury [to creditors]" are not to be disallowed or subordinated. Comstock v. Group of Institutional Investors, 335 U.S. 211, 228-29(1948); see also Small v. Williams, 313 F.2d 39, 42 (4th Cir. 1963) ("Neither in law nor in equity . . . is there any rule of general impropriety in the extension of credit by a dominant stockholder to his corporation" as long as there is "good faith in the effectuation [and] in the implementation of the transaction."). Similarly, in Anaconda Bldg. Materials Co. v. Newland, 336 F.2d 625 (9th Cir. 1964), the court considered the ability of a corporate parent's creditors to reach the assets of the parent's financial subsidiaries. The parent, a builder of prefabricated homes, had formed four subsidiaries to sell debentures in order to raise cash. The funds were used to buy the parent's mortgages at a discount. The parent then used the money in its construction business. Id. at 626-27. The court, affirming the decision of the court below on a "clearly erroneous" standard, declined to permit creditors of the parent to reach the assets of the subsidiaries because (i) the subsidiaries were operated as separate entities; (ii) on balance, the parent was the beneficiary of the corporate relationship; (iii) the objecting creditors did not rely upon the credit of the subsidiaries and were benefited rather than prejudiced by the way in which the subsidiaries were

Furthermore, based on the facts and assumptions contained herein, it would be very difficult for a creditor of Exelon or EEDC to demonstrate reasonable reliance on the assets or credit of Holdco, Pepco Holdings or the Pepco Holdings Utilities or for a creditor of Holdco to demonstrate reasonable reliance on the assets or credit of Pepco Holdings or the Pepco Holdings Utilities. We also believe that it is unlikely that such a creditor could contend justifiably that the organizational structure of the Exelon Entities, Holdco, Pepco Holdings and the Pepco Holdings Utilities misled creditors by making it appear that they were one unit or other than separate units, that the affairs of the Exelon Entities, Holdco, Pepco Holdings and the Pepco Holdings Utilities were so entangled that it would be too costly or time consuming to deal with them separately, or that it appeared that the assets of Holdco, Pepco Holdings or the Pepco Holdings Utilities were available to meet claims of the creditors of one of the Exelon Entities or the assets of Pepco Holdings or the Pepco Holdings Utilities were available to meet claims of the creditors of Holdco. Accordingly, the affairs and assets of the Exelon Entities, Holdco, Pepco Holdings and the Pepco Holdings Utilities would not be commingled or entangled in a way that substantive consolidation is warranted or would benefit all creditors. Creditors of Exelon have relied on Exelon's identity as a legal entity separate from Holdco.[27] Similarly, creditors of Pepco Holdings and the Pepco Holdings Utilities have relied on Pepco Holdings and the Pepco Holdings Utilities' identity as legal entities separate from the Exelon Entities and Holdco.[28] Thus, creditors have dealt with Exelon, Pepco Holdings and the Pepco Holdings Utilities as separate entities, relied on their separateness, and certain creditors would undoubtedly be prejudiced by substantive consolidation of either Holdco with one of the Exelon Entities or of Pepco Holdings or any of the Pepco Holdings Utilities with Holdco or the Exelon Entities. Based on the above, we believe that a court should not consolidate Holdco with either of the Exelon Entities or Pepco Holdings or the Pepco Holdings Utilities with Holdco or either of the Exelon Entities under the Second Circuit test described above, which has been adopted by the Ninth Circuit in In re Bonham or the test adopted by the Third Circuit in In re Owens Corning.

As outlined below, we believe that at least five of seven listed Vecco Construction criteria (numbers 1, 2, 3, 4 and 7) and three of the additional criteria referred to in Eastgroup (numbers 2, 3 and 4) have no substantial application to the present case. The other factors, although present to some extent, are not, in our view, significant enough in the present situation to cause a court to order substantive consolidation of Holdco with Exelon and/or EEDC or of Pepco Holdings or the Pepco Holdings Utilities with Holdco or either of the Exelon Entities, particularly in light of all of

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operated; (iv) there was no fraud or overreaching attributable to the subsidiaries or the debenture holders detrimental to the objecting creditors; and (v) there was no unjust enrichment of the debenture holders. Id. at 628.

[27] You have advised that EEDC does not have any creditors.

[28] You have advised that Holdco does not have any creditors.

the facts described above supporting the separateness of the Exelon Entities, Holdco, Pepco Holdings and the Pepco Holdings Utilities.

With regard to the first of the Vecco Construction factors, the primary business functions of Pepco Holdings and the Pepco Holdings Utilities are, and under regulatory constraints, may only be, performed by Pepco Holdings or the Pepco Holdings Utilities, as applicable. Any overlapping of the assets or business functions of the Exelon Entities with those of Holdco, Pepco Holdings or the Pepco Holdings Utilities or of Holdco with Pepco Holdings or the Pepco Holdings Utilities is incidental and significantly offset by the fact that the other companies strictly observe corporate formalities and regulatory requirements vis-à-vis one another and maintain separate books and records for all of their business functions.

With regard to the second factor, as required by regulatory requirements, the individual assets and liabilities of Holdco, Pepco Holdings and the Pepco Holdings Utilities are segregated and kept separate from those of the Exelon Entities and vice versa. Similarly, the individual assets and liabilities of Pepco Holdings and the Pepco Holdings Utilities are segregated and kept separate from those of Holdco and vice versa. Moreover, each of Exelon, Pepco Holdings and the Pepco Holdings Utilities must follow accounting procedures prescribed by the United States Securities and Exchange Commission and by the Federal Energy Regulatory Commission. Although Exelon's consolidated financial statements include assets of Holdco, Pepco Holdings and the Pepco Holdings Utilities, as required under GAAP, Exelon's financial statements are publicly reported together with separate financial statements for Pepco Holdings and the Pepco Holdings Utilities, which clearly disclose the separate assets belonging to Pepco Holdings, the Pepco Holdings Utilities and their subsidiaries. Accordingly, ascertaining the individual assets and liabilities of Pepco Holdings and the Pepco Holdings Utilities should not be unduly difficult.

With regard to the third factor, none of Pepco Holdings or the Pepco Holdings Utilities have provided, and are prohibited under the regulatory orders authorizing the Merger and the Pepco Holdings Utilities' corporate governance principles from providing, any intercorporate guarantees to Holdco or the Exelon Entities on any indebtedness or other obligations of Holdco or the Exelon Entities. Holdco has not provided, and is prohibited under the regulatory orders authorizing the Merger and the Holdco Operating Agreement from providing, any intercorporate guarantees to either of the Exelon Entities on any indebtedness or other obligations of either of the Exelon Entities. Conversely, there have not been and will not be any parent or intercorporate guarantees provided by Exelon Entities on any indebtedness for borrowed money of Holdco, Pepco Holdings or the Pepco Holdings Utilities or by Holdco on any indebtedness for borrowed money of Pepco Holdings or the Pepco Holdings Utilities. Holdco has not held and may not hold itself out or will hold itself out, or will permit itself to be held out, as having agreed to pay or as being liable for the debts of an Exelon Entity. None of Pepco Holdings or the Pepco Holdings Utilities has held itself out nor will hold itself out, or will permit itself to be held out, as having agreed to pay or as being liable for the debts of Holdco or the Exelon Entities.

With regard to the fourth factor, we note that (i) all arrangements and agreements between and among, the Exelon Entities, Holdco, Pepco Holdings and the Pepco Holdings Utilities have been and will continue to be evidenced by written arrangements or agreements containing arm's-length terms as described above, (ii) there will be no transfers of assets without observance of corporate formalities and accurate recordkeeping, and (iii) the parties will maintain appropriate records in order to be able to ascertain and segregate their respective assets.

With regard to the fifth factor, we note that although consolidated financial statements will be prepared for Exelon and its subsidiaries, including Pepco Holdings and the Pepco Holdings Utilities, the annual reports on Form 10-K and quarterly reports on Form 10-Q have and will continue to include Pepco Holdings and the Pepco Holdings Utilities' separate financial statements. Thus, Pepco Holdings and the Pepco Holdings Utilities will continue to prepare separate financial statements which clearly disclose the separate assets belonging to Pepco Holdings and the Pepco Holdings Utilities and their subsidiaries. In our view, the factor concerning consolidated financial statements relates to the ease of separating assets and liabilities and, more importantly, the equitable consideration of whether the creditors of the different corporations viewed them as one entity. As noted above, Pepco Holdings and the Pepco Holdings Utilities' assets and liabilities can be easily separated from those of the Exelon Entities and Holdco and have been and will be reported to regulators of Pepco Holdings and the Pepco Holdings Utilities, to the financial markets and to creditors of Pepco Holdings and the Pepco Holdings Utilities as such.

With regard to the sixth factor, there is a substantial unity of interests between Exelon and Holdco in that Exelon indirectly owns 100% of Holdco's common equity interests through EEDC. As noted above, Holdco has issued a non-economic share to Member B, which restricts the right of Holdco to take certain bankruptcy-related actions. There is also a substantial unity of interests between Holdco and Pepco Holdings in that Holdco owns 100% of Pepco Holdings' membership interests. The courts have in any event recognized a distinction between the ownership of a subsidiary's equity and of its assets. See In re Beck Indus. Inc., 479 F.2d 410, 415 (2d Cir. 1973), cert. denied, 414 U.S. 858 (1973). We are not aware of any case holding that majority ownership of a subsidiary's stock is sufficient in and of itself to warrant substantive consolidation; were that the case, then the more stringent tests articulated by all of the circuit courts for ordering consolidation would be superfluous. The courts have recognized a distinction between the ownership of an equity interest and of the entity's assets. See footnote 26 and cases cited therein.

The seventh factor should also not result in consolidation. The Exelon Entities have multiple locations dedicated to their own operations, and Holdco, Pepco Holdings and the Pepco Holdings Utilities have multiple locations dedicated their operations. A limited number of officers and employees of Exelon Entities may occupy or use office facilities in locations otherwise dedicated for use by Pepco Holdings and the Pepco Holdings Utilities but will engage in work-activities at those locations on behalf of the Exelon Entities and not as purported officers or employees of Pepco Holdings or the Pepco Holdings Utilities. In addition, some Exelon Entities formerly affiliated with Pepco Holdings may occupy physically separate and secure space as tenants in buildings occupied by Pepco Holdings or the Pepco Holdings Utilities. These arrangements will facilitate the fulfillment of various requirements of regulatory orders authorizing the Merger and will be conducted in accordance with the Ring-Fencing Measures. We are unaware of any other discernable benefit, which would come from allowing the respective entities to share operations on each such location. Moreover, such physical consolidation of operations could be achieved without effecting a substantive consolidation to the detriment of creditors.

The additional factors cited by the Eastgroup court should similarly not be sufficient to warrant consolidation. Although the entities have limited common officers or directors, Holdco's directors, and not the Exelon Entities', are charged with the responsibility of managing the affairs of Holdco. Holdco, Pepco Holdings and the Pepco Holdings Utilities have observed the legal requirements for ensuring that each of Pepco Holdings and the Pepco Holdings Utilities is managed under the supervision of its own board of directors and for otherwise maintaining each of Pepco Holdings and the Pepco Holdings Utilities as a separate entity from Holdco and the Exelon Entities, and vice versa. Many courts have recognized that "it is entirely appropriate for directors of a parent corporation to serve as directors of its subsidiary, and that fact alone may not serve to expose the parent corporation to liability for its subsidiary's acts." U.S. v. Bestfoods, 524 U.S. 51, 69 (1998); see also G-I Holdings, 2001 WL 1598178, at *8 (the court noted that the existence of a common management agreement as to financial, administrative and legal functions, which resulted in overlapping management between corporations, is common in the corporate world and alone is not sufficient for establishing liability).

In light of the above, we would not expect a court to find "substantial identity" based on analyzing the objective factors articulated in Vecco Construction and Eastgroup. Moreover, substantial identity itself is not in and of itself a sufficient ground for consolidation; the court must also find that the benefits of consolidation outweigh the harm. Auto-Train, 810 F.2d at 276; Eastgroup Properties, 935 F.2d at 250. As noted supra, the presence of even several of the Vecco Construction factors does not require substantive consolidation.[29] In the present situation, while certain factors arguably support substantive consolidation, on balance we do not believe that the presence of such factors should warrant substantive consolidation.

2. **Benefit or Harm from Consolidation**

Even if a proponent of substantive consolidation demonstrates a "substantial identity" between the Exelon Entities on the one hand and Holdco on the other hand or between Holdco or the Exelon Entities on the one hand and Pepco Holdings or the Pepco Holdings Utilities on the

[29] See also In re Creditor Serv. Corp., 195 B.R. at 690 (stating that the factors "merely provide the framework" to a court's inquiry and "standing alone, are not dispositive of the issue to consolidate")

other hand (which in each case, as noted above, we do not believe is correct), the proponent must show that substantive consolidation is necessary to avoid some harm or realize some benefit. In the present situation, there does not appear to be any "harm" that needs to be avoided. As discussed above, Holdco has and will consistently hold itself out as an entity separate and distinct from the Exelon Entities and vice versa. Similarly, each of Pepco Holdings and the Pepco Holdings Utilities has and will consistently hold itself out as an entity separate and distinct from Holdco and the Exelon Entities and vice versa. Further, Exelon, Pepco Holdings and the Pepco Holdings Utilities will disclose the existence of Holdco and the implementation of the Ring-Fencing Measures in the Holdco Disclosure Reports, which are and will be publicly available. Creditors of the Exelon Entities and Holdco should therefore have no reasonable basis to allege that they relied on the assets of Holdco as assets of the Exelon Entities (as opposed to the Exelon Entities simply having an equity interest in Holdco) or the assets of Pepco Holdings or the Pepco Holdings Utilities as assets of Holdco or the Exelon Entities (as opposed to Holdco simply having an equity interest in Pepco Holdings). Thus, there does not appear to be any harm that needs to be redressed.

III. Opinion

Based on the foregoing facts and assumptions being correct and continuing to be correct at all relevant times, and subject to the qualifications, limitations and discussion set forth herein and the reasoned analysis of analogous case law (although there is no case directly on point), we are of the opinion that:

(a) in a properly presented and argued proceeding in a case under the Bankruptcy Code in which Exelon and/or EEDC were a debtor, a United States bankruptcy court of competent jurisdiction would not, under applicable federal bankruptcy law, apply the doctrine of substantive consolidation to consolidate the assets and liabilities of Holdco with the assets and liabilities of such debtor; and

(b) in a properly presented and argued proceeding in a case under the Bankruptcy Code in which Holdco, Exelon and/or EEDC were a debtor, a United States bankruptcy court of competent jurisdiction would not, under applicable federal bankruptcy law, apply the doctrine of substantive consolidation to consolidate the assets and liabilities of Pepco Holdings or the Pepco Holdings Utilities with the assets and liabilities of such debtor.

We express no opinion as to the availability or effect of a preliminary injunction, temporary restraining order or other such temporary relief affording delay pending a determination on the merits in the event that substantive consolidation of the assets and liabilities of an Exelon Entity, or Holdco, as applicable, with those of Holdco, Pepco Holdings or the Pepco Holdings Utilities, as applicable, is sought.

In rendering the above opinions, we wish to note that there is no reported controlling judicial precedent directly on point. We therefore examined decisions in which certain of the facts and circumstances set forth in Part I of this opinion were present as well as cases discussing more generally substantive consolidation. Judicial analysis has typically proceeded on a case-by-case basis. The determination is usually made on the basis of an analysis of the facts and circumstances of the particular case, rather than as a result of the application of consistently applied legal doctrines. Existing reported decisional authority is thus not conclusive as to the relative weight to be accorded the factors present in the facts and assumptions set forth in Part I hereof and does not provide consistently applied general principles or guidelines with which to analyze all of the factors present in the facts and assumptions set forth in Part I above.

We have assumed throughout this opinion (i) that there has been no (and will not be any) fraud in connection with the transactions described herein and (ii) the accuracy of the factual matters referred to herein.

Moreover, the authorities we have examined contain certain cases and authorities that are arguably inconsistent with our conclusions expressed herein. These cases and authorities are, however, in our opinion distinguishable in the current context.

This opinion letter relates solely to the Bankruptcy Code and the federal bankruptcy laws of the United States, and thus, we express no opinion as the law of any state. The opinions expressed herein are not a guaranty as to what any particular court would actually hold, but a reasoned opinion as to the decision a court would reach if the issues are properly presented to it and the court followed existing precedent as to legal and equitable principles applicable in bankruptcy cases. Thus, notwithstanding our analysis and conclusions, a court's decision in determining whether substantive consolidation should be ordered is based on its own analysis and interpretation of the factual evidence before it and applicable legal principles. Accordingly, a different conclusion could be reached and would not necessarily constitute reversible error. In this regard, we note that legal opinions on bankruptcy law matters unavoidably have inherent limitations that generally do not exist in respect of other issues on which opinions to third parties are typically given. These inherent limitations exist primarily because of the pervasive equity powers of bankruptcy courts, the overriding goal of reorganization to which other legal rights and policies may be subordinated, the potential relevance to the exercise of judicial discretion of future arising facts and circumstances, and the nature of the bankruptcy process.

This opinion letter is limited to the matters expressly stated herein. No implied opinion may be inferred to extend this opinion letter beyond the matters expressly stated herein.

All of the foregoing analyses and conclusions are premised upon, and limited to, the law in effect as of the date of this opinion.

Our opinions are subject to the effect of general principles of equity, including, without limitation, limitations on the availability of equitable remedies and concepts of materiality, reasonableness, good faith and fair dealing, and other similar doctrines affecting the agreements generally (regardless of whether considered in a proceeding in equity or at law).

This opinion letter is subject to the further qualifications that (i) the assumptions set forth herein are and continue to be true in all material respects and (ii) there are no additional facts that would materially affect the validity of the assumptions and conclusions set forth herein or upon which this opinion letter is based.

We do not undertake to advise you or anyone else of any changes in the opinions expressed herein resulting from the changes in law, changes in facts, or any other matters that hereafter might occur or be brought to our attention.

Very truly yours,

Ballard Spahr LLP

In the Matter of the Petition of Atlantic City Electric Company for a Declaratory Ruling
BPU Docket No. EO21060893
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