CHARLES H. CRUSE
Vice President
Nuclear Energy

Baltimore Gas and Electric Company
Calvert Cliffs Nuclear Power Plant
1650 Calvert Cliffs Parkway
Lusby, Maryland 20657
410 495-4455

BGE

July 31, 1997

U. S. Nuclear Regulatory Commission
Washington, DC 20555

ATTENTION: Director, Nuclear Reactor Regulation

SUBJECT: Calvert Cliffs Nuclear Power Plant
Unit Nos. 1 & 2; Docket Nos. 50-317 & 50-318
Guarantee of Retrospective Premium

In accordance with the requirements of 10 CFR 140.21, we are attaching the guarantee of payment of deferred premiums for our Calvert Cliffs Nuclear Power Plant reactors.

Exhibit I	--	A copy of the 1996 Annual Report to Shareholders of Baltimore Gas and Electric Company containing certified financial statements
Exhibit II	--	A copy of quarterly financial statements as of June 30, 1997
Exhibit III	--	A copy of Projected Cash Flow for the twelve months ended July 31, 1998
Exhibit IV	--	Narrative statement on curtailment/deferment of capital expenditures (if any) to ensure that retrospective premiums up to $10 million per reactor per year for each nuclear incident would be available for payment

Should you have questions regarding this matter, we will be pleased to discuss them with you.

Very truly yours,

CHC/DWM/bjd

Attachment: As stated

1/1
M001

cc: **(Without Attachments)**
Document Control Desk, NRC
R. S. Fleishman, Esquire
J. E. Silberg, Esquire
Director, Project Directorate I-1, NRC
A. W. Dromerick, NRC
T. T. Martin, NRC
Resident Inspector, NRC
R. I. McLean, DNR
J. H. Walter, PSC

Quarterly Financial Summary

June 1997

BGE

CONSOLIDATED STATEMENTS OF INCOME (UNAUDITED)

	Three Months Ended June 30,		Six Months Ended June 30,		Twelve Months Ended June 30,	
	1997	1996	1997	1996	1997	1996
	(In Thousands, Except Per Share Amounts)					
REVENUES						
Electric	$ 498,066	$ 517,780	$ 1,015,362	$ 1,072,224	$ 2,151,883	$ 2,289,546
Gas	92,338	93,515	306,046	312,779	510,558	492,531
Diversified businesses	156,032	120,412*	312,714	208,034	531,891	385,452
Total revenues	746,436	731,707	1,634,122	1,593,037	3,194,332	3,167,529
EXPENSES OTHER THAN INTEREST AND INCOME TAXES						
Electric fuel and purchased energy	112,836	120,704	248,008	274,556	520,866	572,775
Disallowed replacement energy costs	—	6,764	—	6,764	88,605	6,764
Gas purchased for resale	48,167	49,384	181,421	178,412	287,452	265,490
Operations	133,157	130,196	265,031	262,364	529,091	547,047
Maintenance	62,650	60,811	102,195	95,252	181,085	175,278
Diversified businesses—selling, general, and administrative	127,417	84,251	249,047	151,824	408,276	278,651
Write-downs of real estate investments	49,146	—	67,596	—	67,596	—
Depreciation and amortization	85,186	82,332	170,786	167,730	333,246	333,132
Taxes other than income taxes	49,078	48,628	107,323	106,183	215,887	211,890
Total expenses other than interest and income taxes	667,637	583,070	1,391,407	1,243,085	2,632,104	2,391,027
Income from Operations	78,799	148,637	242,715	349,952	562,228	776,502
OTHER INCOME						
Allowance for equity funds used during construction	1,206	2,006	2,416	3,971	4,953	7,933
Equity in earnings of Safe Harbor Water Power Corporation	1,231	1,123	2,461	2,247	4,811	4,591
Net other income and deductions	(1,384)	(1,950)	(2,861)	(4,098)	(3,737)	(8,062)
Total other income	1,053	1,179	2,016	2,120	6,027	4,462
Income Before Interest and Income Taxes	79,852	149,816	244,731	352,072	568,255	780,964
INTEREST EXPENSE						
Interest charges	59,827	53,054	116,114	105,772	227,965	215,151
Capitalized interest	(1,740)	(3,416)	(4,024)	(6,568)	(13,121)	(14,451)
Allowance for borrowed funds used during construction	(653)	(1,083)	(1,306)	(2,146)	(2,680)	(4,289)
Net interest expense	57,434	48,555	110,784	97,058	212,164	196,411
Income Before Income Taxes	22,418	101,261	133,947	255,014	356,091	584,553
INCOME TAXES						
Current	24,799	23,232	68,838	70,131	146,686	139,341
Deferred	(15,467)	15,387	(18,208)	23,372	(15,571)	71,471
Investment tax credit adjustments	(1,883)	(1,911)	(3,764)	(3,823)	(7,595)	(7,857)
Total income taxes	7,448	36,708	46,866	89,680	123,520	202,955
Net Income	14,970	64,553	87,081	165,334	232,571	381,598
Preferred and Preference Stock Dividends	7,874	12,104	15,758	21,768	32,526	42,442
Earnings Applicable to Common Stock	$ 7,096	$ 52,449	$ 71,323	$ 143,566	$ 200,045	$ 339,156
Average Shares of Common Stock Outstanding	147,667	147,527	147,667	147,527	147,618	147,527
EARNINGS PER SHARE OF COMMON STOCK						
Earnings per share from current-year operations:						
Utility business	$0.23	$0.29	$0.62	$0.86	$1.72	$2.06
Diversified businesses*	(0.18)	0.10	(0.14)	0.14	0.03	0.27
Total earnings per share from current-year operations	$0.05	$0.39	$0.48	$1.00	$1.75	$2.33
Disallowed replacement energy costs	—	(0.03)	—	($0.03)	($0.39)	($0.03)
Total earnings per share of common stock	$0.05	$0.36	$0.48	$0.97	$1.36	$2.30

CONSTELLATION COMPANIES*

Revenues	$92,412	$66,769	$160,465	$109,965	$263,343	$225,092
Net Income	(26,301)	13,637	(20,571)	19,457	2,290	37,210
Total Assets--End of Period	1,403,546	1,230,678	1,403,546	1,230,678	1,403,546	1,230,678
BGE's Investment--End of Period	308,773	371,235	308,773	371,235	308,773	371,235

Information for the Constellation Companies does not reflect consolidating eliminations for intercompany balances and transactions.

The interim information contained herein reflects apportionments and estimates of some items subject to final adjustments at the calendar year-end. Results for interim periods, which can be largely influenced by weather conditions, are not necessarily indicative of results to be expected for an entire year.

**1997 results reflect a $0.22 per share real estate write-down in the three-month period and $0.30 per share in real estate write-downs in the six and twelve-month periods.*

CONSOLIDATED BALANCE SHEETS (UNAUDITED)

	June 30, 1997	June 30, 1996
	(In Thousands)	
ASSETS		
CURRENT ASSETS		
Cash and cash equivalents	$ 271,212	$ 38,034
Accounts receivable (net of allowance for uncollectibles of $16,416 and $17,673, respectively)	400,483	418,823
Fuel stocks	80,173	59,240
Materials and supplies	166,320	147,866
Prepaid taxes other than income taxes	3,049	1,953
Deferred income taxes	—	12,810
Trading securities	84,956	64,175
Other	39,051	29,380
Total current assets	1,045,244	772,281
INVESTMENTS AND OTHER ASSETS		
Real estate projects	440,846	496,591
Power generation systems	404,868	364,447
Financial investments	198,037	201,490
Nuclear decommissioning trust fund	128,723	101,871
Net pension asset	96,849	76,108
Safe Harbor Water Power Corporation	34,385	34,334
Senior living facilities	46,351	29,086
Other	99,019	75,550
Total investments and other assets	1,449,078	1,379,477
UTILITY PLANT		
Utility Plant	8,315,395	8,093,821
Accumulated depreciation	(2,715,425)	(2,577,104)
Net utility plant	5,599,970	5,516,717
DEFERRED CHARGES		
Regulatory assets (net)	464,514	610,170
Other	108,475	67,293
Total deferred charges	572,989	677,463
TOTAL ASSETS	$8,667,281	$8,345,938
LIABILITIES AND CAPITALIZATION		
CURRENT LIABILITIES		
Short-term borrowings	$ 116,900	$ 274,845
Current portions of long-term debt and preference stock	324,783	133,953
Accounts payable	147,536	147,859
Customer deposits	28,419	27,447
Accrued taxes	3,247	2,404
Accrued interest	61,356	56,724
Dividends declared	68,402	67,924
Accrued vacation costs	38,872	35,621
Other	23,486	21,645
Total current liabilities	813,001	768,422
DEFERRED CREDITS AND OTHER LIABILITIES		
Deferred income taxes	1,276,242	1,307,231
Pension and postemployment benefits	180,530	155,269
Decommissioning of federal uranium enrichment facilities	38,599	43,694
Other	64,542	70,005
Total deferred credits and other liabilities	1,559,913	1,576,199
CAPITALIZATION		
LONG-TERM DEBT		
First refunding mortgage bonds	1,619,357	1,637,341
Other long-term debt of BGE	937,785	637,000
Long-term debt of Constellation Companies	819,105	561,374
Long-term debt of other diversified businesses	22,000	—
Unamortized discount and premium	(14,317)	(14,911)
Current portion of long-term debt	(221,783)	(94,953)
Total long-term debt	3,162,147	2,725,851
REDEEMABLE PREFERENCE STOCK	216,000	266,500
Current portion of redeemable preference stock	(103,000)	(39,000)
Total redeemable preference stock	113,000	227,500
PREFERENCE STOCK NOT SUBJECT TO MANDATORY REDEMPTION	210,000	210,000
COMMON SHAREHOLDERS' EQUITY		
Common stock	1,431,748	1,425,641
Retained earnings	1,370,778	1,408,437
Net unrealized gain on available-for-sale securities	6,694	3,888
Total common shareholders' equity	2,809,220	2,837,966
Total Capitalization	6,294,367	6,001,317
TOTAL LIABILITIES AND CAPITALIZATION	$8,667,281	$8,345,938

CONSOLIDATED STATEMENTS OF CASH FLOWS (UNAUDITED)

	Six Months Ended June 30,		Twelve Months Ended June 30,	
	1997	1996	1997	1996
	(In Thousands)			
CASH FLOWS FROM OPERATING ACTIVITIES				
Net income	$ 87,081	$165,334	$232,571	$381,598
Adjustments to reconcile to net cash provided by operating activities				
Depreciation and amortization	195,730	191,549	387,336	390,357
Deferred income taxes	(18,208)	23,372	(15,571)	71,471
Investment tax credit adjustments	(3,764)	(3,823)	(7,595)	(7,857)
Deferred energy conservation revenue	—	—	28,500	1,283
Deferred fuel costs	27,738	20,060	8,206	5,648
Disallowance of replacement energy costs	—	6,764	88,605	6,764
Accrued pension and postemployment benefits	(116)	(9,999)	(3,909)	(6,136)
Write-down of real estate investments	67,596	—	67,596	—
Allowance for equity funds used during construction	(2,416)	(3,971)	(4,953)	(7,933)
Equity in earnings of affiliates and joint ventures (net)	(15,604)	(22,944)	(40,965)	(38,624)
Changes in current assets, other than sale of accounts receivable	57,882	26,530	(59,697)	(109,997)
Changes in current liabilities, other than short-term borrowings	(31,943)	(49,651)	13,311	18,536
Other	(816)	23,352	5,103	38,803
Net cash provided by operating activities	363,160	366,573	698,538	743,913
CASH FLOWS FROM FINANCING ACTIVITIES				
Net issuance (maturity) of short-term borrowings	(207,500)	(4,460)	(149,160)	161,345
Proceeds from issuance of				
Long-term debt	519,557	161,346	741,394	335,074
Preference stock	—	—	—	59,329
Common stock	—	—	5,542	212
Proceeds from sale of receivables	—	—	10,000	2,000
Reacquisition of long-term debt	(80,147)	(70,615)	(168,083)	(365,269)
Redemption of preferred and preference stock	(1,500)	(63,559)	(50,500)	(136,559)
Common stock dividends paid	(118,133)	(115,071)	(236,172)	(230,142)
Preferred and preference stock dividends paid	(15,767)	(19,785)	(33,032)	(39,968)
Other	1,201	(436)	(1,349)	(1,004)
Net cash used in financing activities	97,711	(112,580)	118,640	(214,982)
CASH FLOWS FROM INVESTING ACTIVITIES				
Utility construction expenditures (including AFC)	(166,006)	(164,747)	(361,744)	(353,453)
Allowance for equity funds used during construction	2,416	3,971	4,953	7,933
Nuclear fuel expenditures	(17,078)	(15,125)	(48,714)	(45,145)
Deferred energy conservation expenditures	(13,149)	(14,735)	(29,797)	(41,370)
Contributions to nuclear decommissioning trust fund	(8,816)	(16,667)	(17,632)	(21,558)
Costs to achieve the proposed merger	(22,355)	(4,897)	(45,920)	(8,944)
Purchases of marketable equity securities	(9,904)	(22,709)	(19,859)	(34,397)
Sales of marketable equity securities	21,488	24,223	36,922	41,842
Other financial investments	(853)	5,938	278	11,492
Real estate projects	(5,058)	(19,913)	(40,490)	(31,039)
Power generation systems	(18,047)	(9,798)	(21,011)	(30,786)
Other	(19,005)	(4,943)	(40,986)	(12,706)
Net cash used in investing activities	(256,367)	(239,402)	(584,000)	(518,131)
Net Increase (Decrease) in Cash and Cash Equivalents	204,504	14,591	233,178	10,800
Cash and Cash Equivalents at Beginning of Period	66,708	23,443	38,034	27,234
Cash and Cash Equivalents at End of Period	$271,212	$ 38,034	$271,212	$ 38,034
OTHER CASH FLOW INFORMATION				
Cash paid during the year for:				
Interest (net of amounts capitalized)	$100,569	$ 96,790	$191,783	$199,230
Income taxes	$ 57,901	$ 74,759	$141,957	$138,611

Certain prior-year amounts have been restated to conform with the current year's presentation.

UTILITY OPERATING STATISTICS

	Three Months Ended June 30, 1997	Three Months Ended June 30, 1996	Six Months Ended June 30, 1997	Six Months Ended June 30, 1996	Twelve Months Ended June 30, 1997	Twelve Months Ended June 30, 1996
ELECTRIC						
REVENUES *(In Thousands)*						
Residential—with househeating	$ 83,106	$ 88,793	$ 202,167	$ 230,007	$ 395,277	$ 437,294
—other	121,138	130,587	237,875	253,494	520,000	565,588
—total	204,244	219,380	440,042	483,501	915,277	1,002,882
Commercial	213,829	211,657	408,743	403,074	867,011	886,929
Industrial	52,050	52,397	98,555	98,185	207,949	211,271
System sales	470,123	483,434	947,340	984,760	1,990,237	2,101,082
Interchange sales and other sales	22,783	29,333	58,427	77,945	136,359	168,628
Other	5,213	5,220	9,727	9,948	25,272	20,881
Total	$ 498,119	$ 517,987	$1,015,494	$1,072,653	$2,151,868	$2,290,591
SALES *(In Thousands)*—MWH						
Residential—with househeating	974	1,047	2,614	3,032	4,959	5,508
—other	1,272	1,366	2,638	2,820	5,685	6,137
—total	2,246	2,413	5,252	5,852	10,644	11,645
Commercial	2,995	2,970	6,088	6,138	12,541	12,774
Industrial	1,138	1,152	2,263	2,296	4,562	4,661
System sales	6,379	6,535	13,603	14,286	27,747	29,080
Interchange sales and other sales	1,108	1,502	2,863	3,612	6,831	7,996
Total	7,487	8,037	16,466	17,898	34,578	37,076
GAS						
REVENUES *(In Thousands)*						
Residential—with househeating	$ 49,712	$ 45,630	$ 171,889	$ 173,696	$ 279,652	$ 270,847
—other	6,865	7,701	19,358	22,790	35,213	37,397
—total	56,577	53,331	191,247	196,486	314,865	308,244
Commercial						
—excluding delivery service	17,478	20,018	70,405	79,903	115,554	128,045
—delivery service	3,020	1,704	6,915	2,956	11,176	4,796
Industrial						
—excluding delivery service	1,607	2,564	6,557	10,025	13,597	17,316
—delivery service	4,267	4,181	8,384	6,142	16,840	14,110
System sales	82,949	81,798	283,508	295,512	472,032	472,511
Off-system sales	7,486	9,627	18,765	13,328	32,036	13,328
Other	1,903	2,090	3,773	3,939	6,490	6,692
Total	$ 92,338	$ 93,515	$ 306,046	$ 312,779	$ 510,558	$ 492,531
SALES *(In Thousands)*—DTH						
Residential—with househeating	5,893	5,651	21,990	24,569	36,628	39,541
—other	723	829	2,154	2,789	3,941	4,696
—total	6,616	6,480	24,144	27,358	40,569	44,237
Commercial						
—excluding delivery service	2,531	3,432	11,196	14,508	19,387	24,558
—delivery service	2,878	2,254	6,878	3,795	11,838	7,194
Industrial						
—excluding delivery service	366	470	1,175	1,725	2,338	3,452
—delivery service	9,681	9,184	18,766	16,713	38,254	35,278
System sales	22,072	21,820	62,159	64,099	112,386	114,719
Off-system sales	4,035	3,773	9,399	4,658	14,944	4,658
Total	26,107	25,593	71,558	68,757	127,330	119,377

Utility operating statistics do not reflect consolidating eliminations for intercompany transactions.
Certain prior-year amounts have been reclassified to conform with the current year's presentation.

HEATING/COOLING DEGREE DAYS (Calendar-Month Basis)

Heating degree days—Actual	671	597	2,923	3,222	4,840	5,103
—Normal	558	558	3,090	3,120	4,901	4,931
Cooling degree days—Actual	179	279	182	279	689	1,083
—Normal	217	217	220	220	804	804

ELECTRIC GENERATION STATISTICS

	Nuclear	Coal	Oil	Hydro & Gas	Purchased Power Net of Interchange Sales	Total
	Twelve Months Ended June 30,					
Generation by Fuel Type (%)						
1997	42.5	58.4	0.8	3.6	(5.3)	100.0
1996	40.5	57.9	1.7	3.3	(3.4)	100.0
Thousands of MWH						
1997	12,519	17,194	236	1,053	(1,553)	29,449
1996	12,461	17,793	520	1,021	(1,054)	30,741
Average Cost of Fuel (Cents per Million Btu)						
1997	47.11	141.01	299.51	—	—	101.96
1996	46.65	148.06	290.70	—	—	107.77

SUPPLEMENTAL FINANCIAL STATISTICS

	Twelve Months Ended June 30,			
	Utility		Consolidated	
	1997	1996	1997	1996
CAPITALIZATION				
Long-term debt	46.8%	41.9%	50.0%	44.0%
Short-term borrowings	2.2%	5.1%	1.7%	4.3%
Preference stock	7.8%	8.8%	6.3%	7.4%
Common equity	43.2%	44.2%	42.0%	44.3%
RETURN ON AVERAGE COMMON EQUITY				
Reported	8.1%	12.5%	7.0%	12.1%
Excluding disallowed replacement energy costs	10.6%	13.0%	9.1%	12.6%
RATIO OF EARNINGS (SEC Method)				
To fixed charges	2.93	4.00	2.50	3.62
To fixed charges and preferred and preference dividends combined	2.30	2.92	2.05	2.79
AFC as a % of Earnings Applicable to Common Stock	3.9%	4.1%	3.8%	3.6%
Effective Tax Rate	34.5%	34.2%	34.7%	34.7%

COMMON STOCK DATA

	Three Months Ended June 30,		Twelve Months Ended June 30,	
	1997	1996	1997	1996
COMMON STOCK DIVIDENDS PER SHARE				
—Declared	$0.41	$0.40	$1.61	$1.57
—Paid	$0.40	$0.39	$1.60	$1.56
MARKET VALUE PER SHARE				
—High	$27	$28¾	$28¾	$29½
—Low	$24¾	$25½	$25	$24⅜
—Close	$26⅛	$28⅜	$26⅛	$28⅜
Shares Outstanding—End of Period *(In Thousands)*	147,667	147,527	147,618	147,527
Book Value per Share—End of Period	$19.02	$19.24	$19.02	$19.24

Inquiries concerning this summary should be directed to:

David A. Brune
Vice President,
Chief Financial Officer,
and Secretary
(410) 234-5511

Kevin J. Miller
Director,
Financial Planning
(410) 234-5434

Baltimore Gas and Electric Company
P.O. Box 1475
Baltimore, Maryland 21203

Internal Cash Flow Projection
For Calvert Cliffs Nuclear Power Plant

Percentage Ownership in all Operating Nuclear Units	Calvert Cliffs Unit No. 1	100.00%
	Calvert Cliffs Unit No. 2	100.00%

Maximum Total Contingent Liability (000) per Nuclear Incident	$159,000
Payable at Per Year (000)	$20,000

	Twelve Months Ended 6/30/97	Projected Twelve Months Ended 7/31/98
Non - Cash Expenses ($000)		
Depreciation and Amortization	$392,759	$430,877
Deferred Income Taxes and Investment Tax Credits	(13,610)	1,891
Total	$379,149	$432,768
Percentage of Total to Maximum Total Contingent Liability Payable Per Year	1,895.7%	2,163.8%

Retained Earnings ($000)	
Net Income After Taxes	$232,571
Plus Disallowance of Replacement Energy Costs	88,605
Less Allowance for Funds Used During Construction	7,633
Less Dividends paid	269,203
Total	$ 44,340
Total Internal Cash Flow	$423,489
Percentage of Total Internal Cash Flow Maximum Total Contingent Liability Payable Per Year	2,117.4%

Baltimore Gas and Electric Company

Underlying Assumptions for Projected Cash Flows

(1) Projected cash flow does not include an estimate of retained earnings. However, internally generated funds without retained earnings are well in excess of the maximum possible retrospective premiums.

(2) Depreciation is generally computed using composite straight-line rates applied to the average investment in classes of depreciable property. Vehicles are depreciated based on their estimated useful lives.

(3) Estimates of Federal income taxes and other tax expense are based upon existing tax laws and any known changes thereto.

(4) Accounting policies are consistent with those in effect June 30, 1997.

Exhibit IV

Baltimore Gas and Electric Company

Curtailment of Capital Expenditures

Estimated construction expenditures including nuclear fuel, Allowance for Funds Used During Construction, and conservation expenditures for the twelve months ended July 31, 1998 are $407 million. To insure that retrospective premiums under the Price Anderson Act would be available during the aforementioned twelve month period without additional funds from external sources, construction curtailments would affect all construction expenditures rather than impacting a specific project.

Attachment 1
Technical Review Form
Preparation of Regulatory Correspondence

(RM - 1 - 100 Revision 0)

In accordance with the requirements of 10 CFR 140.21 for the Guarantee of Retrospective Premium, for Calvert Cliffs Units Nos. 1 & 2 and the Independent Spent Fuel Storage Installation; Docket Nos. 50-317 & 50-318, certain documents must be submitted to the Nuclear Regulatory Commission. Exhibits 1 & 2 have previously been prepared, reviewed, and approved.

Documentation for the preparation, review, and approval of Exhibits III and IV are shown below

Date

Exhibit III - Internal Cash Flow Projection

Actual data prepared by:
Actual data reviewed by:

Projected data prepared by:
Projected data reviewed by:

Exhibit IV - Curtailment of Capital Expenditures

Projected data prepared by:
Projected data verified by:

The internal cash flow projected reflect the most recent information and are the best estimates available as of the date shown above.

Behind every customer. . .

1996 ANNUAL REPORT

BGE

BGE at a Glance

As the nation's oldest gas utility and one of the earliest electric utilities, the Baltimore Gas and Electric Company brings gas and electricity to more than 2.6 million residents in Central Maryland. BGE's four main subsidiaries also enhance customer service and increase revenue growth. In 1996 combined revenues totaled $3.2 billion from utility and diversified operations.

In September 1995 BGE signed an agreement to merge with Potomac Electric Power Company (Pepco) to form Constellation Energy™ Corporation, one of the 10 largest utilities in the United States. The merger is awaiting regulatory approvals.

Electric
Provides electricity and related services to more than one million customers in a 2,300-square-mile area of Central Maryland. The company owns and operates 10 generating plants, including two nuclear units. Our total generating capacity exceeds 6,200 megawatts.

Gas
Serves more than 555,000 customers in about a 600-square-mile area in Central Maryland. We provide storage and distribution as well as commercial transmission through two gas plants and nine gate stations in and around Baltimore.

Constellation™ Holdings, Inc.
Consists of Constellation Power, Constellation Investments, Constellation Real Estate, and Constellation Health Services. These businesses are involved in the development, ownership, and operation of power generation projects; financial investments; and the development, ownership, and management of real estate and senior-living facilities.

BGE Energy Projects & Services, Inc.
Provides a broad range of customized energy services to commercial and industrial customers. Among its business lines are power quality services, electrical system improvements, lighting and mechanical engineering and installation, district energy systems, and private electric and gas distribution systems.

BGE Home Products & Services, Inc.
Sells and services residential and commercial customers' electric and gas appliances and heating and air-conditioning systems, and offers home improvement services to residential customers.

Constellation Energy Source, Inc. (formerly BNG, Inc.)
Is in the natural gas brokering business, locating, purchasing, and arranging for transmission of gas for large industrial, commercial, and residential customers.

Contents

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More Reader-Friendly Financials
In 1996 BGE became the first utility to sign up for the Securities and Exchange Commission's "Plain English Program," which aims to make investor communications clearer and easier to read. See page 20 for details.

Visit Us on Our Website at http://www.bge.com
There you'll find financial and merger information, as well as the latest residential and business products and services BGE has to offer.

Committed to Equal Opportunity
As an Equal Opportunity Employer, BGE does not discriminate on the basis of age, color, disability, marital status, national origin, race, religion, sex, sexual orientation, or veteran status.

Behind every customer...

When BGE's predecessor, the Gas Light Company of Baltimore, began in 1816, it had a few thousand dollars in assets, five unusually able men, and one bright idea—to light the city. Thanks to the strength of one team of people committed to serve just one customer, the City of Baltimore, this company realized a vision to become the first to bring gaslight to America.

a team of BGE employees

Today, our vision has grown much broader and more brilliant than this pioneering team could have imagined. With Constellation Energy in our future, we are well on our way to becoming one of the largest energy companies in the nation.

Yet as we did 180 years ago, we know our success rests on the strength of our team to serve each customer. Longtime BGE customer Diane Lewandowski, pictured on our cover, understands that. And last fall, during National Customer Service Month, Diane dropped us a note just to tell us how we're doing.

"Over the 25 years I've been a BGE customer, your employees have always been courteous, and have responded beautifully to every request and problem," says Diane. "I know there are so many employees whose work is never recognized, and I just wanted to say thank you."

Our goal is to have every customer feel that way.

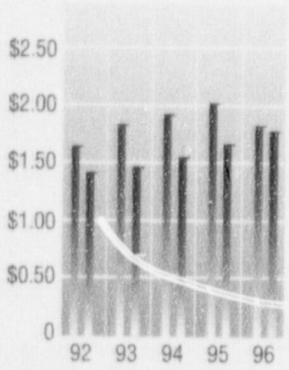
It's a goal we've strived for since the beginning. Behind Diane on our covers are four white-marble figures symbolizing light, heat, knowledge, and power. For 80 years these "Ladies of Lexington Street" have adorned the facade of our company headquarters. They represent the cornerstones of our enduring commitment to our customers.

Highlights

In millions, except per-share amounts	1996	1995	% Change
Common Stock Data			
Earnings per share			
Earnings per share from current-year operations			
Utility business	$1.96	$1.84	6.5%
Diversified businesses	0.31	0.18	72.2%
Total earnings per share from current-year operations	$2.27	$2.02	12.4%
*Disallowed replacement energy costs	(0.42)	–	–
Total earnings per share	$1.85	$2.02	(8.4)%
Dividends declared per share	$1.59	$1.55	2.6%
Average shares outstanding	147.6	147.5	0.1%
Return on average common equity			
Reported	9.5%	10.8%	(12.0)%
*Excluding disallowed replacement energy costs	11.7%	10.8%	8.3%
Book value per share—year end	$19.35	$19.07	1.5%
Market price per share—year end	$26¾	$28½	(6.1)%
Financial Data			
Revenues			
Electric business	$2,209	$2,230	(0.9)%
Gas business	517	400	29.3%
Diversified businesses	427	305	40.0%
Total revenues	$3,153	$2,935	7.4%
Net income	$311	$338	(8.0)%
Earnings applicable to common stock	$272	$297	(8.4)%
Assets			
Utility business	$7,150	$7,051	1.4%
Diversified businesses	1,401	1,266	10.7%
Total assets	$8,551	$8,317	2.8%
Utility construction expenditures (excluding AFC)	$349	$344	1.5%
BGE investment in the Constellation Companies	$396	$352	12.5%
Utility System Data			
Electric sales—megawatt-hours	28.4	28.2	0.7%
Gas system sales—dekatherms	114.3	110.8	3.2%

**A nonrecurring charge to earnings discussed in Note 12 to the Consolidated Financial Statements.*

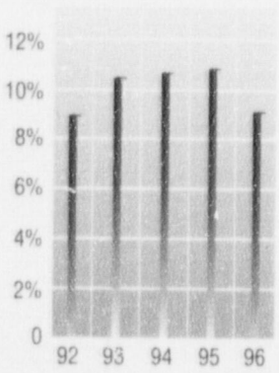
Earnings and Dividends Declared per Share of Common Stock



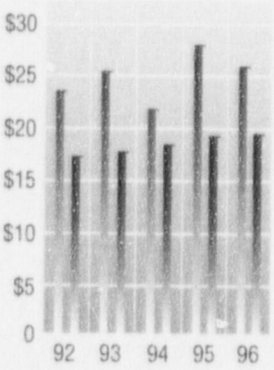
Earnings (Consolidated)

Dividends Declared

Return on Average Common Equity



Common Stock Market Price and Book Value



Market Price (Year-End Close)

Book Value (Year End)

Chairman's Letter To Shareholders

"The farther backward you can look, the farther forward you are likely to see." Winston Churchill knew that tomorrow's strategies are apparent to those who practice the art of the long view. Rewinding through 180 years, we see clearly that the events rocking our industry today are just the latest in a long evolution.

Once again the energy industry is in the throes of consolidation. And once again we are creating a stronger company by forming an alliance with a neighbor utility. This time our merger partner is the Potomac Electric Power Company (Pepco). Constellation Energy Corporation is the new company we are forming through our proposed merger. I've summarized the rationale for the merger and the status of the regulatory approval process on pages 7 and 8.

This report illustrates a year of exceptional teamwork. More than 400 BGE men and women served on teams with their Pepco counterparts to build the framework of Constellation Energy. The rest of our people kept us moving forward on all fronts. Our employees also gave this company a big vote of confidence when they chose to remain union free following an intense union organizing campaign.

Shown from left: George C. Creel, Executive Vice President and Acting Chief Operating Officer; Christian H. Poindexter, Chairman of the Board and Chief Executive Officer; and Edward A. Crooke, President and Chief Operating Officer.

We owe these, and the many other successes of last year, to the quality of our people. Nowhere was quality more evident than in the leadership shown by President and Chief Operating Officer Edward A. Crooke and Executive Vice President and Acting Chief Operating Officer George C. Creel. Along with his Pepco counterpart John M. Derrick, Ed guided the transition teams through the many complex tasks needed to create Constellation Energy Corporation. As Acting Chief Operating Officer, George kept BGE running well and guided our union-free campaign.

Taken together, our efforts strengthened the value of your investment in BGE. We also cleared our financial picture by resolving two long-standing cases with the Maryland Public Service Commission. The cases concerned outages at our Calvert Cliffs Nuclear Power Plant between 1987 and 1991. The resolutions, which we consider fair, resulted in a $62-million, noncash charge to 1996 after-tax earnings.

Here's a brief recount of how your investment in BGE performed last year.

- Earnings from current-year operations equaled $334 million, or $2.27 per share. That's a 12-percent increase over 1995 before the 42-cents-per-share, nonrecurring charge to settle the Calvert Cliffs fuel rate cases.
- BGE's Board of Directors voted to increase the annual dividend to $1.60, up 2.6 percent over last year. This marked our 87th straight year of paying dividends. Also, we have never reduced our dividends.
- We continued to strengthen our dividend payout ratio. Before the Calvert Cliffs settlement, the payout ratio at year end 1996 would have been 70 percent, a sizable improvement from an 88-percent ratio in 1992.
- Earnings from diversified businesses totaled $45.7 million, representing a 73-percent increase over 1995.

Competition Heats Up

On the federal and state levels, regulators continue to wrestle with how best to offer customers a choice of energy suppliers. The 105th Congress will also be considering the issue of electric industry restructuring. One of our key goals is to make sure that our representatives understand the unique issues facing our industry.

The Federal Energy Regulatory Commission (FERC) continued to expand competition in the wholesale power market. Last year the FERC ruled that public and investor-owned utilities must open their transmission lines to competitors. The FERC also required members of power pools to offer service to all users on the same terms as pool members. BGE's power pool, the Pennsylvania-New Jersey-Maryland Interconnection (PJM), has offered to make this service available on March 1, 1998, subject to the FERC's approval of the terms being proposed by the pool members.

States Move at Different Speeds

In 1996 state regulators continued to move at different speeds toward full competition. As of the date of this letter, four states had passed laws that will give all customers a choice of energy providers, while 10 had okayed pilots that will allow the industry to test how a fully open electric market could work.

Maryland's regulators reopened their case and are evaluating when and how to restructure the electric market. The Commission Staff is expected to issue its report this May.

Last year BGE won approval from the Commission to conduct a residential gas pilot program. This follows about a decade of changing regulation on the gas side of our business aimed at opening the natural gas market to competition. Under the plan, which begins in November 1997, 25,000 of our customers will select their own natural gas suppliers.

Gas Targets Strong Growth

Clearly we are at a critical juncture in our gas business's 180-year-old history. We have responded with increasingly ambitious goals for gas growth in our territory. Leading that effort is Frank O. Heintz, who

officially took over as BGE's Vice President, Gas, on January 1, 1997.

Chairman of the Maryland Commission for 13 years, Frank presided over the restructuring of the state's gas industry. After leaving the Commission in 1995, Frank worked with the American Gas Association on high-level issues affecting the gas industry. Frank is a true visionary whose leadership abilities Ed and I have admired for years.

Learning to Differentiate Customers

Increasing customer choice has galvanized our efforts around the dual goals of customer growth and retention. This calls for a much more detailed knowledge about the different categories of customers we serve. We look at all the factors that affect their decision making. How much energy do they use? How sophisticated is their equipment? What competitive pressures do they face? With this knowledge, we can give our customers the advice they need to get the best value for their energy dollars.

Just as it is important that we understand our customers' businesses, we believe it is equally important that our customers understand our business. To that end, last year we conducted a number of seminars and field trips to help our customers understand both the competition in our industry and the issues we face in providing them the reliable service they want. Large industrial customers, hospitals, and military organizations are just a few of the customer groups to which we reached out in 1996.

Going National in 1997

As we move both BGE and Pepco to Constellation Energy, we plan to establish a national brand that will help us market niche products and services that have broad appeal. We are evaluating our positioning and will move forward with the Constellation Energy branding to strengthen our marketing efforts in targeted areas.

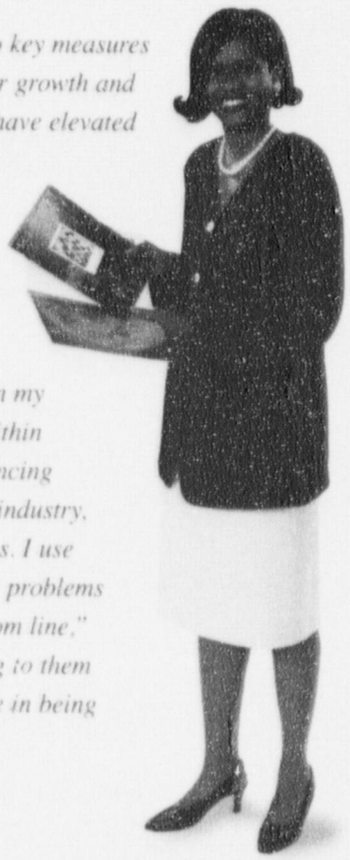
Increasing competition has also caused us to evaluate more closely our strengths and shortcomings. Take reliability as one example. Our residential customers see this as a strong BGE positive, rating BGE nearly 20 percent higher than the industry average for customer satisfaction.

We still have some work to do to with our industrial and commercial customers, however. Recognizing that these customers are affected by both momentary and sustained outages, we set out to reduce those last year. Focusing on 100 key industrial and commercial customers, we decreased their outages 25 percent compared with 1995.

Price is another key success factor in the national energy market. Our employees have been unrelenting in improving the areas that most affect our ability to compete on price. They have raised operating efficiency, increased generating output, and lowered expenses. As a result, BGE is now among the lowest cost generators in its regional comparison group, the PJM power pool.

Growing Diversified Businesses

While competition squeezes profit margins on the sale of natural gas and electricity, it also offers new and promising opportunities for growth and



In an open market, two key measures of success are customer growth and retention, factors that have elevated the role our sales representatives play in ensuring excellent customer relations. National Account Executive Danielle Williams explains, "I'm my customers' advocate within BGE. I'm always enhancing my knowledge of their industry, business and operations. I use this knowledge to solve problems and improve their bottom line," says Danielle, "proving to them that there is extra value in being a BGE customer."

profitability in nonregulated businesses. In fact, within days of signing this letter, I expect to announce the formation of Constellation Power Source, Inc., a subsidiary that will give BGE a substantial presence in the emerging power-marketing business.

Constellation Power Source will buy and sell electric power and related derivatives, develop risk management strategies, and offer a wide array of products that help customers gain greater control of their energy costs. It will draw upon the risk management and trading expertise of one of the world's most prestigious investment banks, Goldman, Sachs & Co., through an exclusive advisory relationship with its subsidiary, Goldman Sachs Power.

Charles W. Shivery has been elected President and Chief Executive Officer of Constellation Power Source, which will be a wholly owned subsidiary of BGE. Chuck has served as BGE's Chief Financial Officer and Corporate Secretary as well as Vice President, Finance & Accounting. Chuck's leadership abilities, financial acumen, and his connections in both the electric and investment banking industries make him the ideal person to guide this venture.

Chuck Shivery, President and Chief Executive Officer of Constellation Power Source, Inc., our newest subsidiary, spent the latter part of 1996 developing a strategic plan for BGE's entry into the electric power marketing and risk-management business. "Constellation Power Source combines the strengths of two top-notch organizations—BGE's 180-years of excellence in the energy industry with the unparalleled financial risk-management expertise of Goldman Sachs," Chuck says. This advisory relationship—the first of its kind in the power-marketing industry—puts us in a superb position to benefit in a deregulated environment."

Employees Work With Forces of Change

In 1996 Ed, George, and I clocked a lot of hours speaking to our employees about our changing industry. I am thankful that our employees recognized that it is better to work with the forces of change rather than working against them by voting for a union. More than 70 percent of employees whose votes were counted chose to preserve the advantage BGE has as a nonunion company in a unionized industry. There is no doubt in my mind that we are a stronger, more focused company for having gone through this experience.

Commitment to Shareholder Value

I believe our shareholders, too, are aware of the way our industry is changing. That's why 97 percent of those who voted favored the merger. Our plans are to model Constellation Energy's dividend policy after BGE's—that is, with an emphasis on consistency and appropriate growth.

Obviously a more competitive market dictates a greater need to reinvest in the business to provide growth opportunities, and indeed our payout ratio has decreased. We are achieving the goal not by decreasing the dividend but by increasing our earnings. We plan to continue as an excellent yield-oriented investment, funding dividend increases through earnings growth.

On behalf of our entire team, I thank you for your continued faith in the Baltimore Gas and Electric Company. We look forward to making the transition to Constellation Energy Corporation in the near future.

Christian H. Poindexter

Chairman of the Board and
Chief Executive Officer
February 18, 1997

This historic merger not only strengthens our position in the increasingly competitive energy industry, it also ensures that the energy products and services we offer our customers in the future will be among the best in the country.

a winning combination

Mergers Gain Momentum

As of the date of this letter, 17 proposed mergers await FERC approval. Several represent the combination of large electric and gas companies. That bears out what BGE has been saying for 90 years: There is a competitive advantage in being able to deliver both gas and electricity. It also lends credibility to speculation that the leaders of the energy industry of the future will be larger companies, created through consolidations.

This sharp increase in the number of proposed mergers caused the FERC to revisit its 30-year-old merger policy. The FERC will now concentrate its evaluation of each merger on the merger's effect on competition, on rates, and on state and federal regulation. This merger policy will be applied on a case-by-case basis to pending mergers.

A Seamless Shift for Constellation Customers

Both BGE and Pepco have excellent reputations for quality customer service, reputations the Customer Relations Activity Team set out to preserve when we become Constellation Energy Corporation. Made up of a diverse group of BGE and Pepco employees, team members had one thing in common: Every one of them was an experienced problem solver who knew how to successfully handle customer concerns.

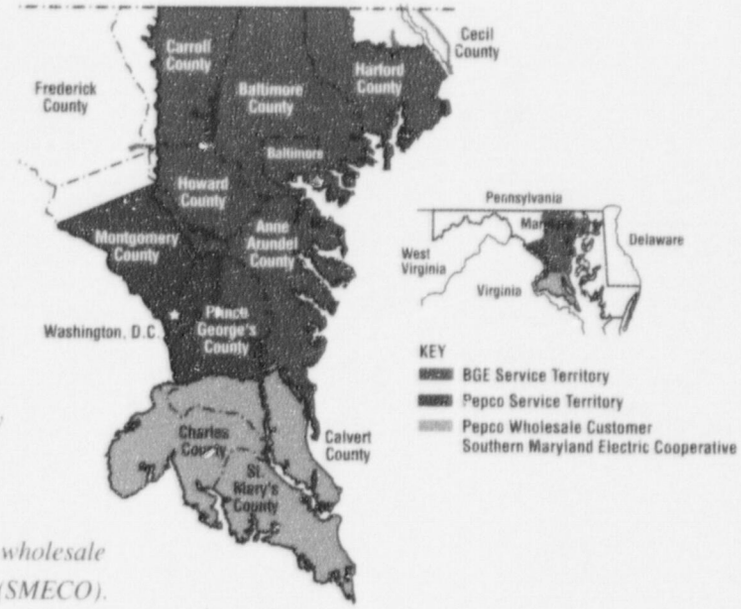
The team's mission was to research our current methods and those used by best-practice companies, then recommend ways to bridge the transition from two companies to one. "Sure there were differences in the way the companies operated," says Pepco's leader Joy Cole. "But we were all driven by the same common goal—to provide seamless service to Constellation's customers."

"It's a job that was made easier," adds BGE's leader Mary Ellen January, "by the fact that we were able to pool our resources and talents and stay focused on our customers." Shown from left: Terry Gastfield, Rose Darone, Carolyn Cardwell, John Disney, Joy Cole, William Latlief, Priscilla Savoy, Robert Atkins III, and Mary Ellen January.

As a combined company with over $15 billion in assets, Constellation Energy will be among the 10 largest electric utilities in the United States, serving a diverse population of more than 1.8 million electric customers and more than 555,000 gas customers.

Constellation Energy will be structured as a single utility with subsidiaries conducting the nonutility operations. Its service territory will encompass all or part of 10 Maryland counties, Baltimore City, and Washington, D.C.—virtually all of Central Maryland, including the entire Baltimore-Washington corridor.

Constellation Energy will also sell electricity at wholesale to the Southern Maryland Electric Cooperative (SMECO).



Approvals Progressing

Regarding FERC approval of the BGE-Pepco merger, all required documents have been submitted, all hearings have been completed, and we are awaiting an approval. The same applies to the approvals needed from the Maryland Commission.

The merger also requires the approval of the District of Columbia Public Service Commission, which has postponed until late February 1997 hearings originally scheduled for early December 1996. All documentation will be submitted by mid-March. We expect the D.C. Commission to rule on these matters promptly thereafter.

Merger Strengthens Customer Focus

Achieving cost savings is one of the prime motivations behind our merger with Pepco. We estimate the merger will save $1.3 billion over the first 10 years. In April 1996, we filed our joint merger application with the Maryland and D.C. Commissions, proposing that our shareholders and customers share those savings and that we increase our already strong commitment to the community.

Customers will reap the benefits of improved operations as well. The merger will allow us to keep rates lower than we could as a stand-alone company. It will increase reliability at our common borders and create a better customer mix. And, given our coal, nuclear, and gas resources, the merger will also result in a more balanced fuel mix that will help us enhance price stability in changing markets.

Commitment to Community Will Continue

A larger but still locally based energy company will also better serve the needs of the community at large. The BGE-Pepco merger does not disadvantage local interests. Our corporate headquarters will be located in Maryland's capital city, Annapolis, and we will maintain significant concentrations of employees in both Baltimore and Washington.

Both BGE and Pepco are regarded as excellent corporate citizens. As individual companies, each is known throughout the Baltimore-Washington area for its commitment to economic development, corporate philanthropy, low-income customer initiatives, and volunteerism. Together, as Constellation Energy Corporation, we will remain steadfast in that commitment.

Energy has come a long way...

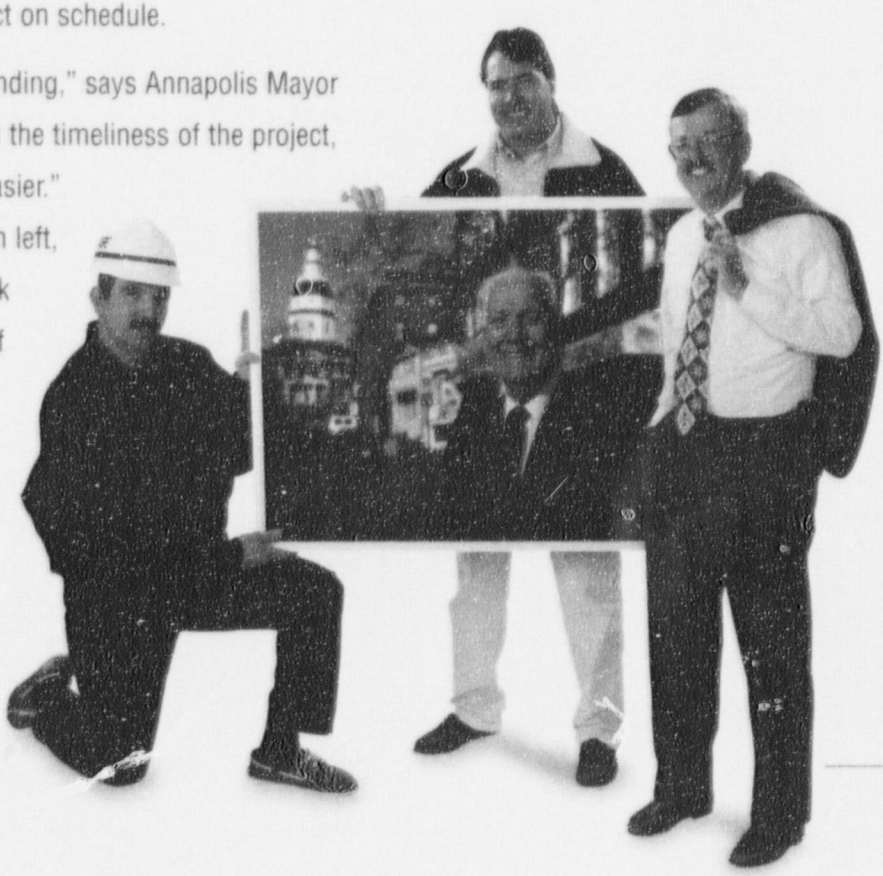
On the pages that follow, you'll see some images from our past, mixed in with our 1996 highlights. They remind us that we have inherited an important legacy from those who preceded us: improving the lives of the people we serve.

and so have we

Our job was not easy in the "good old days." Workers lacked the powerful technology and machinery we take for granted today. As this photo shows, laying electric cable circa 1900 was no small feat. Yet our archives are full of pictures of proud men and women doing whatever they needed to do to get the job done.

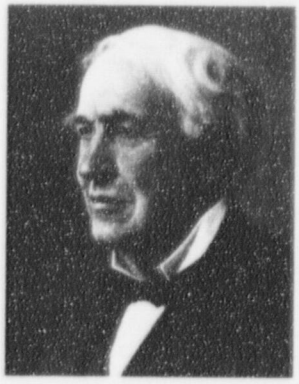
Contrast that with one of our best teamwork stories of 1996: our role in renovating Annapolis, Maryland's state capital. As part of the $5.5 million upgrade of its historic Main Street District, the City of Annapolis asked BGE to put all electric lines underground and to replace and update gas lines. Employees from both the gas and electric sides of our company worked on a fast track to complete the project on schedule.

"BGE's crews were absolutely outstanding," says Annapolis Mayor Al Hopkins (inset). "They understood the timeliness of the project, and they made all of our jobs a lot easier." Included on the BGE team were, from left, Terry Bowen, Gas Construction; Frank Elliott, Customer Operations; and Jeff Jefferson, Public Affairs.



While our equipment and the methods are drastically different, the heart of our company remains the same. Now, as then, teams of employees working together to give our customers the best possible service—a legacy we'll continue at Constellation Energy

Behind every customer...

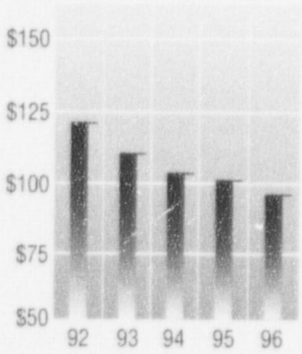


In 1997 we celebrate the 150th anniversary of the birth of Thomas Alva Edison, the father of the Electric Age. Because of his innovations, BGE has been providing electricity to a growing base of customers for much of our long history.

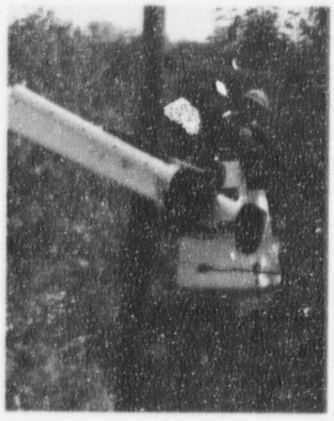
Now, as competition moves into the marketplace, we're setting aggressive goals to remain among the industry's leaders. To write a new chapter in our history, we've been working to reduce generating costs, deliver reliable electric service, provide energy products and services that meet customers' needs, and successfully compete in the bulk-power market. Here are some of our accomplishments for the year.

Since 1992 we've reduced operations and maintenance costs at our fossil-fueled power plants by nearly $28 million. Those reductions have been driven by continuous improvement processes, such as cross-training employees in both operations and maintenance activities.

Fossil Generating Costs Down 24% in Five Years
Millions of Dollars



- Our cost reduction efforts helped us continue to generate competitively priced power. BGE is among the lowest cost producers of electricity in its regional comparison group, the PJM power pool.
- Last year our generation employees also set new records for working safely. In both our Fossil and Nuclear divisions, our employees had the lowest occupational injury rate in BGE generation history.
- New technologies and an aggressive predictive maintenance program helped us produce an additional 426,000 megawatt hours at our eight key fossil-fueled power plants. We finished the year producing more than 18 million megawatt hours, an all-time record for our fossil plants.
- In 1996 our Calvert Cliffs Nuclear Power Plant generated 12.1 million megawatt hours—the fourth highest generation total in the plant's history.
- Calvert Cliffs also earned the highest marks in three of four categories assessed by the Nuclear Regulatory Commission (NRC). The plant earned superior ratings in engineering, operations, and plant support. The NRC also noted improvement in the plant's maintenance.
- A new operating strategy implemented last year is helping us reduce expenses and the time it takes to return customers' service during storm-related outages. The improvements moved our dispatchers and system operators to a central location during storms, giving them better, more direct access to needed storm system data.



Employees like Dewane Daley are helping BGE prepare to compete successfully. As project manager of our Distribution System Power Quality Assessment Project, Dewane oversees the installation of special meters that track disturbances in our power supply to industrial customers. "One thing that will set us apart is electric service our industrial customers can trust," says Dewane. "Knowing where we stand now in terms of power quality will give us an edge in tomorrow's competitive electric market."

- We intensified our reliability efforts by establishing a Reliability and Power Quality Master Plan. It is a broad-based program to develop system infrastructure changes that improve reliability and power quality. This year we also focused our reliability efforts on our industrial and commercial customers.
- To make the transition to the emerging competitive bulk-power market, we're continuing to expand our efforts to market wholesale electricity. In 1996 our Bulk Power Arrangements Group made great strides as they engaged in over 12 million megawatt hours of wholesale purchases and sales of electricity.

Responding Rapidly to Electric Needs

Behind Al Reid (inset) is a team of BGE Customer Operations employees working to meet his electric needs. Reid is president of Rapid Response, a direct-mail marketing business that depends on sensitive electronic equipment to produce customized brochures. Last year a power surge caused Rapid Response to lose critical information from its databases, and caused Reid to call BGE.

In response, he got a whole team. Helen Handy, Special Investigator-Customer Operations, received the information on Rapid Response from our Customer Communications Center. Her initial analysis revealed a reliability problem. She turned that information over to John Mathews, an Assistant Distribution Technician who went into the field and found the problem—faulty insulators on the power lines that supply Rapid Response. The work order then went to Al Leightner, a Distribution Construction supervisor, who along with crew members Gary Diffenderfer and Bob Fogle, Jr., quickly repaired the line and put Rapid Response back in business.

"When BGE learned about our power problem and how critical it was for us to find a permanent solution, an expert team arrived the next day," says Reid. "I was impressed with the response, and I was impressed with the results."

Shown from left: John Mathews, Bob Fogle, Jr., Al Leightner, Helen Handy, and Gary Diffenderfer.

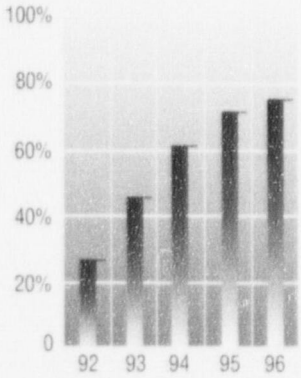
Behind every customer...

When artist and entrepreneur Rembrandt Peale lit a gas-powered light in his Baltimore museum in 1816, he planted a seed that's still growing today. Peale's successful demonstration of the value of gas led to the founding of the Gas Light Company of Baltimore, our forerunner. From that modest start, BGE has developed a gas business that continues to expand rapidly in a competitive energy marketplace.

With more customers demanding natural gas in their homes and businesses, we've developed aggressive, profitable growth strategies to meet their needs. Over the next couple of years, we plan to continue to increase the number of new residential, commercial, and industrial customers we serve, and to capitalize on the value of home gas-heat comfort and other gas applications. This year we made great strides in our gas growth, including the following.

Continuing an excellent five-year growth trend, we again significantly increased our share of the new home-heating market. More than 9,000 of the new houses built in Central Maryland last year connected to our gas system, establishing a new market penetration record of 72 percent.

Gas Increases Share of New Home Market



- In our continuing effort to expand our gas business, we converted almost 6,000 residential customers to natural gas heat last year.
- Measuring our growth in miles, the gas system grew by 339 miles in 1996, giving us a total of nearly 5,400 miles of gas mains serving about 555,000 customers in Baltimore City and nine Maryland counties.
- In October we began a market-based rates program approved by the Maryland Commission. The new program provides earnings opportunities and financial incentives for BGE to reduce the cost of buying gas and to share the savings with our customers.
- We began sales of off-system gas during the first quarter of 1996. The Maryland Commission approved an arrangement permitting shareholders to keep a portion of the earnings on these sales.
- Our Gas Construction employees teamed with the Gas Research Institute, the gas industry's leading research and development organization, in a pilot program testing new applications for flexible gas pipes. The pilot has reduced average installation time from six hours to under one hour, a significant benefit in lowering installation costs. We plan to begin using the new flexible pipe regularly in 1997.
- We're looking to further improve gas sales to large customers through several initiatives. First, we're educating architectural and engineering firms about the benefits of choosing

gas equipment for their industrial and commercial customers. We also began an advisory group with several of our larger customers, including Johns Hopkins Hospital, General Motors, and Maryland's Department of General Services. The group provides a forum to address customer needs and concerns on natural gas issues.

- Last year we began retiring the last three of our huge steel gas holders, which are memorials to the earliest days of our gas supply. With their retirement, we're saving nearly $1 million per year in operations and maintenance costs and an additional $7 million that would have been spent for a scheduled maintenance.

Frank O. Heintz, BGE's new Vice President, Gas, brings a top-level view of the emerging competitive gas industry, thanks to his 13 years as Chairman of the Maryland Public Service Commission. "Growth is our foremost strategy," says Frank. "We're growing by positioning ourselves to take advantage of new opportunities and by finding better ways to deliver gas and service to the customer."

Extending Ourselves to Meet Gas Demand

Teamwork is helping us quickly meet customer demand for natural gas. Take the case of AAI Corporation, a defense contractor and light rail manufacturer. When it was awarded a contract to build car shells for several light rail systems, AAI needed to quickly build a paint booth, and BGE needed to quickly extend a gas main for it.

Enter Keith Brock, Energy Sales & Services. Knowing AAI was on a fast track to meet the contract, Keith took it upon himself to pour a concrete pad to accommodate the meter needed for AAI's new booth. That done, employees from Gas Engineering and Construction, led by supervisor Lee Cavey and crew members Tim Wilson and Charles Kelly, took over with the digging and welding needed to extend the main and install the metering equipment.

Together, the team finished the job in time for AAI to meet its deadline, which included a planned celebration with the governor for the rollout of the first car. "We were impressed with BGE's commitment to get the job done on time," said AAI facility engineer Steve Brodbeck (inset). "They went above what you'd normally expect from a utility."

Shown from left: Tim Wilson, Keith Brock, Lee Cavey, and Charles Kelly.

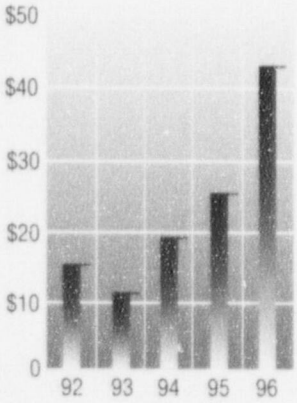
Behind every customer...

A century ago fierce competition forced many energy companies into a struggle for survival. To rise above the rest, Baltimore's dominant electric company and its largest gas company made the bold decision to merge in 1906, forming the area's first combined gas and electric company.

Ninety years later utilities again find themselves facing competitive challenges. By combining the talents of the utility and its subsidiaries, BGE holds an advantage as it moves forward. In 1996 our subsidiary operations both increased overall profitability and helped strengthen ties with our customers. Here are a few highlights.

BGE's diversified business earnings were $45.7 million, a 73-percent increase over 1995 thanks to a strong performance by Constellation Holdings.

Diversified Earnings Nearly Tripled Since 1992
Millions of Dollars



Constellation Holdings

- Constellation Power strengthened its niche in the domestic energy market while it expanded its interests in Latin America.
- *Power* magazine and *Power Engineering* magazine named Constellation's Colver Power Project in Pennsylvania the 1996 Power Plant of the Year.

Bolivia's Valle Hermoso Power Plant, one of Constellation Power's Latin American investments.

- In Hawaii the Puna Geothermal Project expanded its generating capacity. It now provides nearly 25 percent of the electrical power used on the Big Island.
- Constellation Investments cashed in on strong financial markets to post record earnings, paced by excellent results from its marketable securities program and investments in financial partnerships.
- Constellation Real Estate's asset and property management division merged with KLNB Management Services to form Constellation Realty Management, the largest company of its kind in the Baltimore region.
- Constellation Health Services continued to expand. It now has investments in 520 of the more than 2,000 senior-living units it manages and is developing more than 700 additional units.

BGE Energy Projects & Services

- Serving large commercial customers throughout the Mid-Atlantic region, BGE Energy Projects & Services' projects included such things as lighting retrofits for retail stores in five states; energy system upgrades for several U.S. Post Offices; and installation of a portable turf-heating system for Baltimore's new NFL team, the Ravens.

- PowerDigm Systems®, Inc., provides power quality products and services to utilities and other large electric users. In 1996 the company signed five contracts for its PowerDigm® Transfer℠ system, a technology that can dramatically improve power quality. It also launched its PowerDigm Automation℠ service line to help utilities improve power quality through distribution and substation automation.

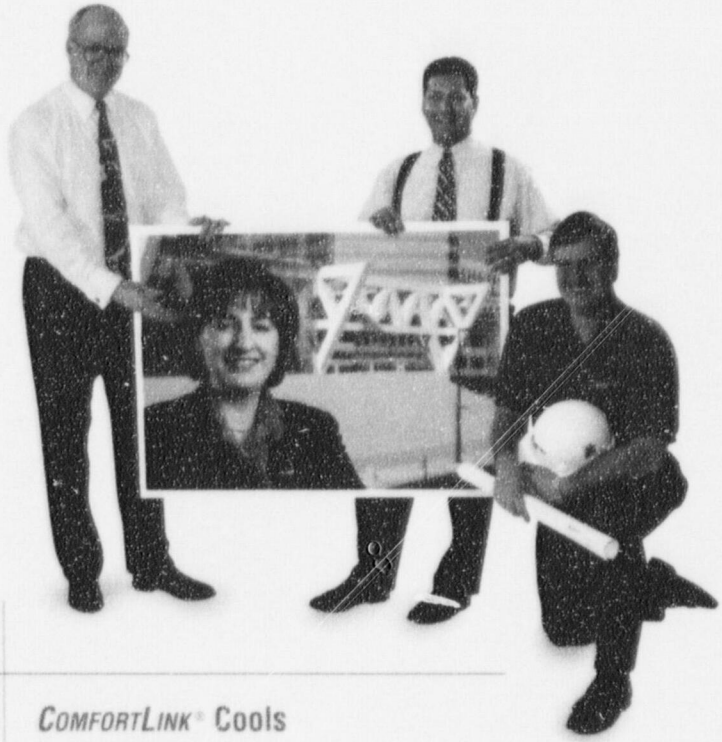
BGE Home Products & Services

- BGE Home Products and Services (HP&S) continues to meet residential and commercial customers' high demand for quality products and services. One of the biggest growth areas in 1996 has been assisting local commercial customers with their building systems. For example, when Baltimore City Schools needed to overhaul their heating systems, they turned to HP&S' Commercial Services Team to help solve their problem.

Constellation Energy Source

- In the past year, BGE's gas-marketing subsidiary changed its name from BNG to Constellation Energy Source. It also established itself in three regions of the country to launch its gas-marketing effort. By the year 2000 it plans to have a major presence throughout the U.S.

Patti Lovelady, Vice President, Constellation Energy Source, runs the daily operations of our gas-marketing subsidiary at a time when the whole industry is breaking new ground. "The future of the industry is ***energy*** *marketing, not just gas, oil, or electricity marketing. I see Constellation Energy Source playing a key role in our full-service efforts," says Patti.*



ComfortLink® Cools Convention Center

When Baltimore expanded its Convention Center last year, *ComfortLink*—a partnership between BGE and The Poole & Kent Company—offered the Center's executive director Peggy Daidakis (inset) a great deal: Let us build our first central cooling plant there, and then reap the benefits of low-cost air conditioning for years to come.

Thanks to Dennis Manning, Greg Fox, Poole & Kent's Bill Parsons, and the rest of the *ComfortLink* team, the Convention Center now houses the plant. And more downtown businesses have recognized its advantages. *ComfortLink* now has agreements to cool nine buildings, including Oriole Park at Camden Yards, the Ravens' new football stadium, and two of Fidelity & Deposit Company of Maryland's office buildings.

ComfortLink is designed to use central facilities to pump hot and cold water beneath city streets to heat and cool downtown Baltimore buildings.

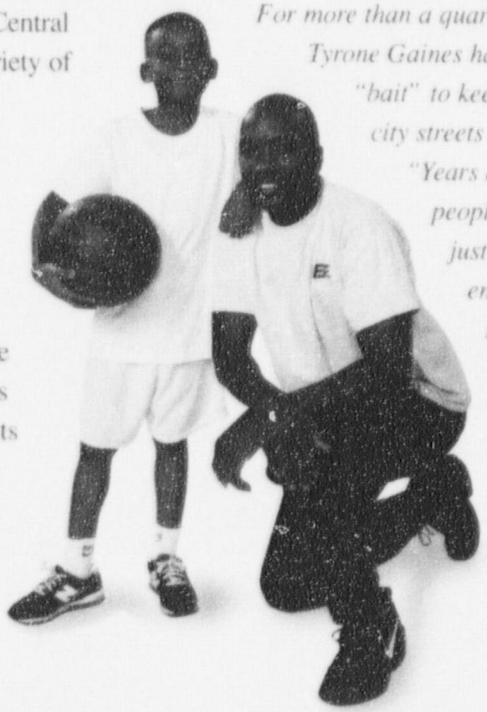
Shown from left: Bill Parsons, Greg Fox, and Dennis Manning.

Behind every customer... a leading corporate citizen

On December 1, 1958, BGE President J. Theodore Wolfe rolled up his sleeve to donate the first unit to BGE's blood program. Today as then, we recognize that the vitality of our company depends on the well-being of the communities we serve. In 1996 we rolled up our sleeves to strengthen the economic, environmental, and social fabric of Central Maryland. The results are nothing less than dramatic.

- BGE has a long-standing commitment to business growth and retention, job creation, and economic expansion in Maryland. That's why we began offering an Economic Development Discount to businesses for relocating or expanding in Central Maryland. Sixteen companies have already signed on for these temporary electric-price reductions, bringing an estimated 1,600 jobs to our area. Chesapeake Biological Laboratories is but one example.

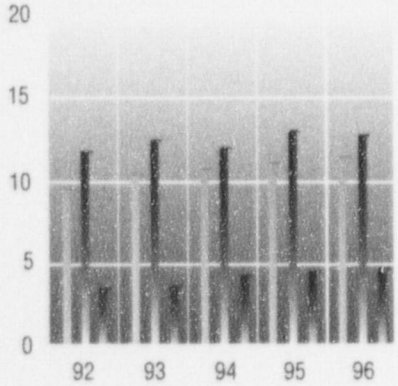
- Our desire to improve the quality of life for the members of the communities we serve is what drives our corporate-giving program. In 1996 we remained the largest corporate giver in Central Maryland, granting $4.3 million to a variety of nonprofit groups. A major focus of our corporate giving is early childhood development, a cause we see as an investment in Maryland's future.
- With rapid technological change altering the state of local industry, a highly skilled and adaptable work force is more critical than ever to Maryland's economic strength. BGE awarded grants to six of Maryland's community colleges to help Maryland citizens acquire the skills needed in today's high-performance workplaces.
- Our employees have always been our greatest asset, and we are constantly encouraging them to take their talents and expertise beyond the walls of our company. More than 6,000 BGE employees and retirees volunteered over 9,100 hours of their own time in 1996, raising a total of $1.4 million for charity through our Employee Volunteer Program.
- As an industry leader in pollution prevention, BGE has created a balance between the need to provide safe, reliable, and economical energy service and the need to protect the environment. Last year our efforts earned us two WasteWi$e Awards from the Environmental Protection Agency. We recycled 60 percent of our solid waste, saving the company $5.7 million.



For more than a quarter of a century, Tyrone Gaines has used basketball as "bait" to keep hundreds of kids off city streets and away from crime. "Years ago, when I heard people saying, 'If you could just save one,' that wasn't enough—I wanted to save them all," says the BGE Volunteer of the Year. "But now I realize that saving that one is phenomenal."

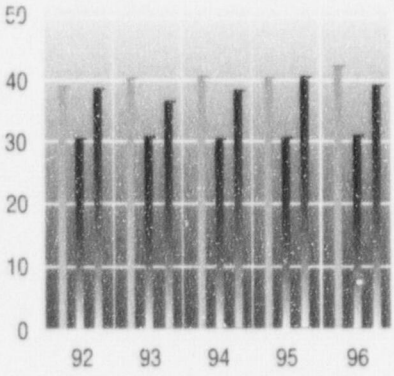
Financial Contents

Sales of Electricity
Billions of Kilowatt-Hours



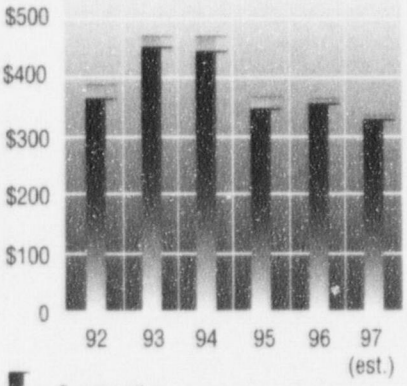
Residential
Commercial
Industrial

Sales of Gas
Millions of Dekatherms



Residential
Commercial
Industrial

Utility Construction Expenditures
Millions of Dollars



Construction
Allowance for Funds Used During Construction

Utility Operating Statistics

	1996	1995	1994	1993	1992	Compound Growth 5-Year	Compound Growth 10-Year
Electric Operating Statistics							
Revenues *(In Thousands)*							
Residential	**$ 958,736**	$ 955,239	$ 931,711	$ 931,643	$ 839,954	1.67%	5.23%
Commercial	**861,343**	879,438	852,989	869,829	842,694	0.26	3.49
Industrial	**207,579**	208,441	205,611	199,042	201,950	(0.50)	0.77
System Sales	**2,027,658**	2,043,118	1,990,311	2,000,514	1,884,598	0.83	3.93
Interchange and Other Sales	**155,877**	166,964	118,027	91,543	64,323	45.57	5.26
Other	**25,492**	21,029	19,083	20,090	16,611	3.44	8.07
Total	**$2,209,027**	$2,231,111	$2,127,421	$2,112,147	$1,965,532	2.10	4.05
Sales (In Thousands)–MWH							
Residential	**11,243**	10,966	10,670	10,614	9,735	2.17	3.73
Commercial	**12,591**	12,635	12,351	12,395	11,909	1.47	2.98
Industrial	**4,596**	4,591	4,433	3,763	3,663	4.39	1.26
System Sales	**28,430**	28,192	27,454	26,772	25,307	2.19	2.96
Interchange and Other Sales	**7,580**	8,149	5,684	4,149	3,180	45.41	6.57
Total	**36,010**	36,341	33,138	30,921	28,487	6.18	3.62
Customers							
Residential	**995,197**	988,179	978,591	968,212	956,570	1.15	1.54
Commercial	**104,501**	103,399	101,957	100,820	99,673	1.24	1.99
Industrial	**4,261**	4,161	3,967	3,800	3,761	3.52	5.38
Total	**1,103,959**	1,095,739	1,084,515	1,072,832	1,060,004	1.17	1.60
Average Use per Residential Customer–KWH	**11,297**	11,097	10,903	10,963	10,177	1.01	2.15
Average Rate per KWH (System Sales)–¢							
Residential	**8.53**	8.71	8.73	8.78	8.63	(0.49)	1.46
Commercial	**6.84**	6.96	6.91	7.02	7.08	(1.18)	0.48
Industrial	**4.52**	4.54	4.64	5.29	5.51	(4.67)	(0.47)
Peak Load (One-Hour)–MW	**5,955**	5,947	6,038	5,876	5,558	0.15	2.58
Capability at Summer Peak–MW	**6,800**	6,731	6,722	6,701	6,687	0.57	1.61
System Load Factor	**57.5%**	57.2%	54.7%	55.2%	54.8%	1.87	0.21
Gas Operating Statistics							
Revenues *(In Thousands)*							
Residential	**$ 320,105**	$ 248,283	$ 262,736	$ 265,601	$ 242,737	7.73	2.14
Commercial							
Excluding Delivery Service	**125,052**	109,859	121,005	121,832	112,147	5.39	(0.03)
Delivery Service	**7,217**	3,696	2,285	3,287	3,591	18.95	9.83
Industrial							
Excluding Delivery Service	**17,064**	16,730	20,140	22,250	21,123	6.57	(3.55)
Delivery Service	**14,598**	16,332	9,635	12,920	14,290	(4.69)	(3.23)
System Sales	**484,036**	294,900	415,801	425,890	393,888	6.76	1.14
Off-System Sales	**26,600**	—	—	—	—	—	—
Other	**6,656**	5,604	5,448	7,273	6,511	(0.36)	(6.90)
Total	**$ 517,292**	$ 400,504	$ 421,249	$ 433,163	$ 400,399	7.77	1.50
Sales (In Thousands)–DTH							
Residential	**43,784**	40,211	40,279	40,029	39,042	3.70	1.26
Commercial							
Excluding Delivery Service	**22,698**	23,612	23,712	23,830	23,478	1.87	0.49
Delivery Service	**8,755**	6,982	6,490	7,428	7,102	6.36	6.55
Industrial							
Excluding Delivery Service	**2,887**	4,102	4,410	5,298	5,314	(4.34)	(6.39)
Delivery Service	**36,201**	35,925	33,837	31,390	33,638	1.12	3.01
System Sales	**114,325**	110,832	108,728	107,975	108,574	2.41	1.62
Off-System Sales	**10,204**	—	—	—	—	—	—
Total	**124,529**	110,832	108,728	107,975	108,574	4.18	2.49
Customers							
Residential	**516,523**	506,739	498,152	491,165	486,863	1.39	0.69
Commercial	**38,861**	38,422	37,891	37,518	37,000	1.23	1.23
Industrial	**1,350**	1,334	1,354	1,353	1,412	(0.51)	0.42
Total	**556,734**	546,495	537,397	530,036	525,275	1.37	0.72
Average Use per Residential Customer–Therms	**848**	794	809	815	802	2.27	0.57
Average Rate per Therm–$							
Residential	**.73**	.62	.65	.66	.62	4.00	0.86
Commercial (Excluding Delivery Service)	**.55**	.47	.51	.51	.48	3.64	(0.53)
Industrial (Excluding Delivery Service)	**.59**	.41	.46	.42	.40	11.61	3.16
Peak Day Sendout–DTH	**708,966**	706,287	761,900	657,700	609,200	3.05	1.27
Peak Day Capability–DTH	**870,000**	847,000	847,000	847,000	847,000	1.27	[illegible]

Utility operating statistics do not reflect the elimination of intercompany transactions.

Selected Financial Data

	1996	1995	1994	1993	1992	Compound Growth 5-Year	Compound Growth 10-Year
	(Dollar amounts in thousands, except per share amounts)						
Summary of Operations							
Total Revenues	**$3,153,247**	$2,934,799	$2,782,985	$2,741,385	$2,559,536	4.63%	4.63%
Expenses Other Than Interest and Income Taxes	**2,483,782**	2,239,107	2,147,726	2,124,993	2,024,227	4.15	5.21
Income From Operations	**669,465**	695,692	635,259	616,392	535,309	6.54	2.73
Other Income	**6,130**	8,819	32,365	20,310	22,132	(26.25)	(9.83)
Income Before Interest and Income Taxes	**675,595**	704,511	667,624	636,702	557,441	5.55	2.49
Net Interest Expense	**198,438**	196,977	190,154	188,764	189,747	0.19	5.82
Income Before Income Taxes	**477,157**	507,534	477,470	447,938	367,694	8.37	1.39
Income Taxes	**166,333**	169,527	153,853	138,072	103,347	14.22	1.65
Net Income	**310,824**	338,007	323,617	309,866	264,347	4.17	1.25
Preferred and Preference Stock Dividends	**38,536**	40,578	39,922	41,839	42,247	(2.05)	3.67
Earnings Applicable to Common Stock	**$ 272,288**	$ 297,429	$ 283,695	$ 268,027	$ 222,100	5.26	0.95
Earnings Per Share of Common Stock	**$1.85**	$2.02	$1.93	$1.85	$1.63	2.07	(1.26)
Dividends Declared Per Share of Common Stock	**$1.59**	$1.55	$1.51	$1.47	$1.43	2.58	3.03
Ratio of Earnings to Fixed Charges	**3.10**	3.21	3.14	3.00	2.65	6.43	(2.97)
Ratio of Earnings to Fixed Charges and Preferred and Preference Stock Dividends Combined	**2.44**	2.52	2.47	2.34	2.08	6.04	(2.68)
Financial Statistics at Year End							
Total Assets	**$8,550,970**	$8,316,663	$8,037,502	$7,829,613	$7,208,660	3.68	6.44
Capitalization							
Long-term debt	**$2,758,769**	$2,598,254	$2,584,932	$2,823,144	$2,376,950	2.91	5.62
Preferred stock	**—**	59,185	59,185	59,185	59,185	—	—
Redeemable preference stock	**134,500**	242,000	279,500	342,500	395,500	(19.53)	10.40
Preference stock not subject to mandatory redemption	**210,000**	210,000	150,000	150,000	110,000	13.81	6.68
Common shareholders' equity	**2,857,113**	2,812,682	2,717,866	2,620,511	2,534,639	5.82	5.77
Total Capitalization	**$5,960,382**	$5,922,121	$5,791,483	$5,995,340	$5,476,274	3.12	5.63
Book Value Per Share of Common Stock	**$19.35**	$19.07	$18.42	$17.94	$17.63	2.62	3.43
Number of Common Shareholders	**77,550**	79,811	81,505	82,287	80,371	1.74	0.07

Management's Discussion and Analysis of Financial Condition and Results of Operations

Introduction

In Management's Discussion and Analysis we explain the general financial condition and the results of operations for BGE and its diversified business subsidiaries including:

- what factors affect our business,
- what our earnings and costs were in 1996 and 1995,
- why those earnings and costs were different from the year before,
- where our earnings came from,
- how all of this affects our overall financial condition,
- what our expenditures for capital projects were in 1994 through 1996 and what we expect them to be in 1997 through 1999, and
- where cash will come from to pay for future capital expenditures.

As you read Management's Discussion and Analysis, it may be helpful to refer to our Consolidated Statements of Income on page 31, which present the results of our operations for 1996, 1995, and 1994. In Management's Discussion and Analysis, we analyze and explain the annual changes in the specific line items in the Consolidated Statements of Income. Our analysis may be important to you in making decisions about your investments in BGE.

You may notice some changes in this year's discussion, compared to past years. This is because we volunteered to participate in a pilot program with the Securities and Exchange Commission to write financial documents in plain English. As a result, we have re-written our entire Management's Discussion and Analysis section. Our goal is to discuss our financial condition in language that is more easily understood.

BGE and Potomac Electric Power Company have agreed to merge into a new company named Constellation Energy Corporation. We plan to complete the merger as soon as we obtain all regulatory approvals. These matters are discussed in more detail in Note 12 beginning on page 48 and in a Registration Statement on Form S-4 (Registration No. 33-64799). The merger may impact many of the matters discussed in Management's Discussion and Analysis including earnings, results of electric operations, expenses, liquidity, and capital resources.

The electric utility industry is undergoing rapid and substantial change. Competition is increasing. The regulatory environment (federal and state) is shifting. These matters are discussed briefly in the "Competition and Response to Regulatory Change" section on page 22 in Management's Discussion and Analysis. They are discussed in detail in our Annual Reports on Form 10-K. BGE continuously evaluates these changes. Based on the evaluations, BGE refines short and long term business plans with the primary goal of protecting our security holders' investments and providing them with superior returns on their investment in BGE. In order to support this primary goal, we also focus on other groups who impact our primary goal. For example, we stress providing low cost, reliable power to our electric customers. As you read Management's Discussion and Analysis, many BGE initiatives to support our primary goal are mentioned. These include the proposed merger with Potomac Electric Power Company, designed to position us to remain competitive as the industry changes, and our diversification effort. We enter new businesses which we believe will support our primary goal. For example, new businesses may be opportunities to:

- provide customers of our core energy business additional services, or
- attract new customers for our core energy business, or
- expand our diversified stream of revenues.

We believe our newest subsidiary, Constellation Power Source, Inc., will satisfy all three criteria. Its proposed power marketing business is described in detail in the front of this report.

Results of Operations

In this section, we discuss our 1996 and 1995 earnings and the factors affecting them. We begin with a general overview, then separately discuss earnings for the utility business and for diversified businesses.

Overview

Total Earnings per Share of Common Stock

	1996	1995	1994
Earnings per share from current-year operations:			
Utility business	$1.96	$1.84	$1.81
Diversified businesses (subsidiaries)	.31	.18	.12
Total earnings per share from current-year operations	2.27	2.02	1.93
Disallowed replacement energy costs (see Note 12)	(.42)	—	—
Total earnings per share	$1.85	$2.02	$1.93

1996

Our 1996 total earnings decreased $25.1 million, or $.17 per share, from 1995. Our total earnings decreased because we reserved for disallowed replacement energy costs. We discuss this in detail in the "Disallowed Replacement Energy Costs" section on page 23.

In 1996, we had higher utility earnings from current-year operations due to three factors: we sold more electricity and gas due to colder winter weather (people use more gas and electricity to heat their homes in colder weather), there was an increase in the number of customers, and we had lower operations and maintenance expenses. We would have had even higher utility earnings from current-year operations except we sold less electricity in the third quarter due to milder summer weather. We discuss our utility earnings in more detail beginning on page 22.

In 1996, we had higher earnings from our diversified business subsidiaries mostly because the Constellation Companies had higher earnings from power generation projects and financial investments. We discuss our diversified business earnings in more detail beginning on page 26.

1995

Our 1995 total earnings increased $13.7 million, or $.09 per share, from 1994.

In 1995, we had higher utility earnings mostly due to greater sales of electricity during an extremely hot summer and higher electricity and gas sales resulting from colder fall weather. We would have had even higher utility earnings except for the mild weather in the first half of the year, lower net other income and deductions (miscellaneous non-operating income and expenses), and lower allowance for funds used during construction (an accounting procedure used to exclude the cost of capital from expense and include it as part of the cost of utility plant construction).

In 1995, we had higher earnings from our diversified businesses mostly because the Constellation Companies had higher earnings from power generation projects and financial investments.

Utility Business

Before we go into the details of our electric and gas operations, we believe it is important to discuss four factors that have a strong influence on our utility business performance: regulation, the weather, other factors including the condition of the economy in our service territory, and competition.

Regulation by the Maryland Public Service Commission

The Maryland Public Service Commission (Maryland Commission) determines the rates we can charge our customers. Our rates consist of a "base rate" and a "fuel rate". The base rate is the rate the Maryland Commission allows us to charge our customers for the cost of providing them service, plus a profit. We have both an electric base rate and a gas base rate. Higher electric base rates apply during the summer when the demand for electricity is the highest. Gas base rates are not affected by seasonal changes.

The Maryland Commission allows us to include in base rates a component to recover money spent on conservation programs. This component is called an "energy conservation surcharge." However, under this surcharge the Maryland Commission limits what our profit can be. If, at the end of the year, we have exceeded our allowed profit, we lower the amount of future surcharges to our customers to correct the amount of overage, plus interest.

In addition, we charge our electric customers separately for the fuel (nuclear fuel, coal, gas, or oil) we use to generate electricity. The actual cost of the fuel is passed on to the customer with no profit. We also charge our gas customers separately for the natural gas they consume. The price we charge for the natural gas is based on a Market Based Rates incentive mechanism approved by the Maryland Commission. We discuss Market Based Rates in more detail in the "Gas Cost Adjustments" section on page 24 and in Note 1 on page 39.

From time to time, when necessary to cover increased costs, we ask the Maryland Commission for base rate increases. Not every request for base rate increases is granted in full. However, the Maryland Commission has historically allowed BGE to increase base rates to recover costs for replacing utility plant assets, plus a profit, beginning at the time of replacement. Generally, rate increases improve our utility earnings because they allow us to collect more revenue. However, rate increases are normally granted based on historical data and those increases may not always keep pace with increasing costs.

Weather

Weather affects the demand for electricity and gas, especially among our residential customers. Very hot summers and very cold winters increase demand. Mild weather reduces demand.

We measure the weather's effect using "degree days." A degree day is the difference between the average daily actual temperature and a baseline temperature of 65 degrees. Cooling degree days result when the daily actual temperature exceeds the 65 degree baseline. Heating degree days result when the daily actual temperature is less than the baseline.

During the cooling season, hotter weather is measured by more cooling degree days and results in greater demand for electricity to operate cooling systems. During the heating season, colder weather is measured by more heating degree days and results in greater demand for electricity and gas to operate heating systems.

The following chart shows the number of cooling and heating degree days in 1996 and 1995, shows the percentage changes in the number of degree days from prior years, and shows the number of degree days in a "normal" year as represented by the 30-year average.

	1996	1995	30-Year Average
Cooling degree days	786	1,056	804
Percentage change compared to prior year	(25.6)%	11.3%	
Heating degree days	5,138	4,601	4,901
Percentage change compared to prior year	11.7%	(1.5)%	

Other Factors

Other factors, aside from weather, impact the demand for electricity and gas. These factors include the "number of customers" and "usage per customer" during a given period.

The number of customers in a given period is affected by new home and apartment construction and by the number of businesses in our service territory.

Usage per customer refers to all other items impacting customer sales which cannot be separately measured. These factors include the strength of the economy in our service territory. When the economy is healthy and expanding, customers tend to consume more electricity and gas. Conversely, during an economic downtrend, our customers tend to consume less electricity and gas.

We use these terms later in our discussions of electric and gas operations. In those sections, we discuss how these and other factors affected electric and gas sales during 1996 and 1995.

Competition and Response to Regulatory Change

Our business is also affected by competition. Electric utilities are facing competition on three fronts:

- in the construction of generating units to meet increased demand for electricity,
- in the sale of their electricity in the bulk power markets, and
- in the future, for electric sales to retail customers which utilities now serve exclusively.

We regularly reevaluate our strategies with two goals in mind: to improve our competitive position, and to anticipate and adapt to regulatory changes. In September 1995, we decided that a merger with Potomac Electric Power Company would help us compete by maintaining low-cost production and increasing our size. The pending merger is more thoroughly discussed in Note 12 on page 48. Although we believe the merger will improve our competitive position in the future, no one can predict the ultimate effect competition or regulatory change will have on our earnings or on the earnings of the merged company.

We will continue to develop strategies to keep us competitive. These strategies might include one or more of the following:

- the complete or partial separation of our generation, transmission, and distribution functions
- other internal restructuring
- mergers or acquisitions of utility or non-utility businesses
- addition or disposition of portions of our service territories
- spin-off or distribution of one or more businesses

We cannot predict whether any transactions of the types described above may actually occur, nor can we predict what their effect on our financial condition or competitive position might be.

We discuss competition in our electric and gas businesses in more detail in our Annual Reports on Form 10-K under the headings "Electric Regulatory Matters and Competition" and "Gas Regulatory Matters and Competition."

Utility Business Earnings per Share of Common Stock

	1996	1995	1994
Utility earnings per share from current-year operations:			
Electric business	$1.75	$1.70	$1.71
Gas business	.21	.14	.10
Total utility earnings per share from current-year operations	1.96	1.84	1.81
Disallowed replacement energy costs (see Note 12)	(.42)	—	—
Total utility earnings per share	$1.54	$1.84	$1.81

Our 1996 total utility earnings decreased $44.5 million, or $.30 per share, from 1995. Our 1995 utility earnings increased $5.6 million, or $.03 per share, from 1994.

We discuss the factors affecting utility earnings below.

Electric Operations

Electric Revenues

The changes in electric revenues in 1996 and 1995 compared to the respective prior year were caused by:

	1996	1995
	(In millions)	
Electric system sales volumes	$ 0.4	$ 43.4
Base rates	(2.5)	23.2
Fuel rates	(12.3)	(13.8)
Total change in electric revenues from electric system sales	(14.4)	52.8
Interchange and other sales	(11.1)	49.0
Other	4.5	1.4
Total change in electric revenues	$(21.0)	$103.2

Electric System Sales Volumes

"Electric system sales" are sales to customers in our service territory at rates set by the Maryland Commission. These sales do not include interchange sales and sales to others.

The percentage changes in our electric system sales volumes, by type of customer, in 1996 and 1995 compared to the respective prior year were:

	1996	1995
Residential	2.5%	2.8%
Commercial	(0.3)	2.3
Industrial	0.1	3.6

In 1996, we sold more electricity to residential customers for three reasons: colder weather in the first quarter, greater electricity usage per customer, and an increase in the number of customers. We would have sold even more electricity to residential customers except for milder summer weather. We sold about the same amount of electricity to commercial and industrial customers as we did in 1995. As mentioned above, weather impacts residential, more than commercial and industrial, sales. In 1996 other items offset the impact of weather on commercial and industrial sales. Other items include the demand for power to fuel manufacturing equipment and office machinery, which vary with changes in the customers' businesses. For example, if a manufacturing plant has a slow year, it will make less product and use less power to run its assembly lines.

In 1995, we sold more electricity to residential and commercial customers mostly because we had an increase in the number of customers and we had extremely hot summer weather and cold fall weather. We would have sold even more electricity to those customers except we had milder weather in the first half of 1995 compared to 1994. We sold more electricity to industrial customers mostly because we had an increase in the number of customers and more demand for electricity from Bethlehem Steel (our largest customer).

Base Rates

In 1996, base rate revenues were about the same as they were in 1995. Although we sold more electricity this year, our revenues did not increase because the higher sales occurred during the winter when our base rates are lower.

In 1995, base rate revenues were higher than in 1994 because of a higher energy conservation surcharge and also because we did not have to reduce conservation revenues as we did in 1994, when we exceeded our allowed profit.

From July 1, 1993, through June 30, 1994, we exceeded our profit limit under the energy conservation surcharge. To correct the overage, we lowered the surcharge on our customers' bills from December 1993 to November 1994. As a result, we billed $20.1 million less than we would have otherwise. We also exceeded the limit on our profit during 1996. Therefore, we excluded $28.5 million of our 1996 surcharge billings from revenue, and we will lower the surcharge on our customers' bills beginning in July 1997 to correct the overage.

Fuel Rates

The fuel rate is the rate the Maryland Commission allows us to charge our customers for our actual cost of fuel with no profit to us. If the cost of fuel goes up, the Maryland Commission permits us to increase the fuel rate. If the cost of fuel goes down, our customers benefit from a reduction in the fuel rate. The fuel rate is impacted most by the amount of electricity generated at the Calvert Cliffs Nuclear Power Plant because the cost of nuclear fuel is cheaper than coal, gas, or oil. (See Note 1 on page 39 for a further discussion of how the fuel rate increases and decreases.)

Changes in the fuel rate normally do not affect earnings. However, if the Maryland Commission disallows recovery of any part of the fuel costs, our earnings are reduced. (We discuss this more thoroughly in the "Electric Fuel and Purchased Energy Expenses" section below and in Note 12 on page 50.)

In 1996 and 1995, fuel rate revenues decreased due to a lower fuel rate because we were able to operate plants with the lowest fuel costs to generate electricity during the previous 24 months. Fuel rate revenues would have been even lower except we sold more electricity. In 1995, the fuel rate was also lower compared to 1994 because of lower fuel costs.

Interchange and Other Sales

"Interchange and other sales" are sales of energy in the Pennsylvania-New Jersey-Maryland Interconnection (PJM) and to others. The PJM is a regional power pool of eight utility member companies, including BGE. We sell energy to PJM members and to others after we have satisfied the demand for electricity in our own system.

In 1996, we had lower interchange and other sales compared to 1995 because we generated less electricity at our Calvert Cliffs Nuclear Power Plant. This meant that we had less electricity to sell outside of our service territory. We generated less electricity at that plant mostly because the 1996 outage for regular refueling and maintenance took longer than in 1995.

In 1995, interchange and other sales increased because we were able to operate plants with the lowest fuel costs to generate electricity, had available capacity, and had lower costs than other utilities. Specifically, we had greater generation from our coal-fired Brandon Shores Power Plant, and our Calvert Cliffs Nuclear Power Plant generated a record level of electricity during 1995.

Electric Fuel and Purchased Energy Expenses

	1996	1995	1994
		(In millions)	
Actual costs	$539.2	$554.5	$541.2
Net recovery of costs under electric fuel rate clause (see Note 1)	8.2	24.3	1.1
Disallowed replacement energy costs (including carrying charges) (see Note 12)	95.4	—	—
Total electric fuel and purchased energy expenses	$642.8	$578.8	$542.3

Actual Costs

In 1996, our actual cost of fuel to generate electricity (nuclear fuel, coal, gas, or oil) and electricity we bought from other utilities was lower than in 1995 because the price of electricity and capacity we bought from other utilities was lower and we sold less electricity. The price we pay for electricity and capacity we buy from other utilities changes based on market conditions, complex pricing formulas for PJM transactions, and contract terms.

In 1995, our actual cost of fuel to generate electricity and electricity we bought from other utilities was higher than in 1994 mostly because we generated more electricity and the price of electricity and capacity we bought from other utilities was higher. Our actual costs would have been even higher except we were able to use a less-costly mix of generating plants, mostly because of shorter refueling and maintenance downtime at our Calvert Cliffs Nuclear Power Plant.

Electric Fuel Rate Clause

The "electric fuel rate clause" (determined by the Maryland Commission) requires that we defer (to include as an asset or liability on the balance sheet and exclude from income and expense) the difference between our actual costs of fuel and our fuel rate revenues collected from customers through the fuel rate. We bill or refund that difference to customers in the future.

In 1996 and 1995, our actual fuel costs were lower than the fuel rate revenues we collected from our customers. As a result, we recovered fuel costs which we had deferred in prior years.

Disallowed Replacement Energy Costs

During 1989 through 1991 we experienced extended outages at our Calvert Cliffs Nuclear Power Plant. These outages have been the subject of ongoing fuel rate proceedings before the Maryland Commission for several years (see Note 12 on page 50).

In December 1996, we entered into a settlement agreement with the Maryland People's Counsel and the Maryland Commission Staff. We agreed not to bill our customers for $118 million of electric replacement energy costs associated with these extended outages. We set up a reserve for $35 million of these costs in 1990. In 1996, we increased that reserve by $83 million and we wrote off $5.6 million of related carrying charges. In addition, we wrote off $6.8 million of fuel costs that were disallowed by the Maryland Commission in May 1996 (we discuss these costs further in Note 12 on page 50). These write-offs and the increase in the reserve significantly increased our total purchased fuel and energy expenses in 1996. The remainder of the replacement energy costs associated with the extended outage has already been recovered from customers through the fuel rate.

Gas Operations

Gas Revenues

The changes in gas revenues in 1996 and 1995 compared to the respective prior year were caused by:

	1996	1995
	(In millions)	
Gas system sales volumes	$ 8.2	$ 0.2
Base rates	18.9	6.4
Gas cost adjustments	62.1	(27.4)
Total change in gas revenues from gas system sales	89.2	(20.8)
Off-system sales	26.6	—
Other	1.0	0.1
Total change in gas revenues	$116.8	$(20.7)

Gas System Sales Volumes

The percentage changes in our gas system sales volumes, by type of customer, in 1996 and 1995 compared to the respective prior year were:

	1996	1995
Residential	8.9%	(0.2)%
Commercial	2.8	1.3
Industrial	(2.3)	47

In 1996, we sold more gas to residential and commercial customers due to colder winter and early spring weather and an increase in the number of customers. We would have sold even more gas to those customers except that gas usage per customer decreased. We sold less gas to industrial customers because Bethlehem Steel used less gas. We would have sold even less gas to industrial customers except for increased gas usage by other industrial customers, an increase in the number of customers, and colder winter weather.

In 1995, we sold about the same amount of gas to residential customers as we did in 1994. We sold more gas to commercial customers for three reasons: an increase in the number of customers, increased gas usage per customer, and colder weather in the fall of 1995. We would have sold even more gas to commercial customers except for milder weather in the first half of 1995. We sold more gas to industrial customers due to greater gas usage per customer.

Base Rates

In 1996, base rate revenues were higher than in 1995 because in November 1995, the Maryland Commission allowed us to increase our gas base rates. This increased our annual base rate revenues for 1996 by $19.3 million, or approximately 3.7% of total 1996 gas revenues. That amount included $2.4 million to recover higher depreciation expense (an accounting procedure which spreads the cost of utility plant in service over the years in which it is used).

In 1995, our base rate revenues were higher than in 1994 because of the energy conservation surcharge.

Gas Cost Adjustments

Prior to October 1996, the Maryland Commission allowed us to recover the actual cost of the gas sold to our customers through "gas cost adjustment clauses." These clauses require that we defer the difference between our actual cost of gas and the gas revenues we collect from customers. We bill or refund that difference to customers in the future.

Effective October 1996, the Maryland Commission approved a modification of the gas cost adjustment clauses to provide a "Market Based Rates" incentive mechanism. In general terms, under Market Based Rates our actual cost of gas is compared to a market index (a measure of the market price of gas in a given period), and half of the difference belongs to shareholders. We discuss this in more detail in Note 1 on page 39.

Delivery service customers, including Bethlehem Steel, are not subject to the gas cost adjustment clauses because we are not selling them gas (we are selling them the service of delivering their gas).

In 1996, gas cost revenues increased because we had to pay more for gas and we sold more gas. In 1995, gas cost revenues decreased because we paid less for gas and we sold less gas.

Off-System Sales

Off-system gas sales, which are direct sales to suppliers and end users of natural gas outside our service territory, also are not subject to gas cost adjustments. We began sales of off-system gas during the first quarter of 1996. The Maryland Commission approved an arrangement for part of the earnings from off-system sales to benefit customers (through reduced costs) and the remainder to be retained by BGE (which benefits shareholders).

Gas Purchased For Resale Expenses

	1996	1995	1994
		(In millions)	
Actual costs	$295.4	$205.9	$222.7
Net recovery (deferral) of costs under gas adjustment clauses (see Note 1)	(11.0)	(7.8)	1.9
Total gas purchased for resale expenses	$284.4	$198.1	$224.6

Actual Costs

Actual costs include the cost of gas purchased for resale to our customers and for sale off-system. These costs do not include the cost of gas purchased by delivery service customers, including Bethlehem Steel.

In 1996, actual gas costs increased from 1995 due to three factors: higher market prices of gas, higher sales volumes, and the purchase of gas to resell off-system (beginning in the first quarter of 1996).

In 1995, actual gas costs decreased compared to 1994 because of the considerably lower market price of gas. This decrease would have been even greater except that we received supplier refunds in 1994 which reduced actual gas costs that year.

Gas Adjustment Clauses

We charge customers for the cost of gas sold through gas adjustment clauses (determined by the Maryland Commission), as discussed under "Gas Cost Adjustments" earlier in this section.

In 1996 and 1995, the portion of our actual gas costs subject to these clauses was higher than the revenues we collected from our customers. As a result, we deferred the difference and will collect the costs from our customers in the future. These deferrals decreased our total gas purchased for resale expenses in 1996 and 1995.

Other Operating Expenses

Operations and Maintenance Expenses
In 1996, our operations and maintenance expenses decreased $18.5 million due to our continued efforts to control costs. This decrease would have been even greater except we had higher costs to maintain our nuclear plant. In 1995, our operations and maintenance expenses were about the same as they were in 1994.

Depreciation and Amortization Expenses
We describe depreciation and amortization expenses in Note 1 on page 40.

In 1996, our depreciation and amortization expense increased $12.8 million from 1995 for two reasons:

- we had more utility plant in service to be depreciated (as our level of utility plant that is in service changes, the amount of our depreciation expense changes), and
- we had more energy conservation program costs to be amortized.

The increase in these expenses would have been even greater except that in 1995 depreciation and amortization expense included $14.2 million for the write-off of certain costs of our Perryman site, which is covered in more detail below. In 1996, depreciation and amortization expense did not include any such write-off.

In 1995, our depreciation and amortization expense increased $21.5 million over 1994 because we had more utility plant in service to be depreciated (mostly because of some capital additions to our Calvert Cliffs Nuclear Power Plant), and we had a higher level of energy conservation program costs to be amortized. In addition, we completed a study of the cost to decommission Calvert Cliffs. (Decommission is a term used in the nuclear industry for the permanent shut-down of a nuclear power plant which usually occurs when the plant's license expires.) The study resulted in a higher estimated cost of decommissioning, which increased decommissioning expense (included in depreciation and amortization expense) by $9 million annually.

Our 1995 and 1994 depreciation and amortization expense reflected the write-off of expenditures associated with future generation facilities at our Perryman site which will not be built. We discuss the write-off of expenditures at our Perryman site further in Note 1 on page 40. The write-off of these costs increased our 1995 depreciation and amortization expense by $14.2 million and increased our 1994 expense by $15.7 million.

Taxes Other Than Income Taxes
In 1996, taxes (other than income taxes) were $9.6 million higher than in 1995 mostly due to three factors: plant additions made in 1995 increased our property taxes about $7 million, higher 1996 revenues increased our gross receipts taxes about $2 million, and higher labor costs increased our payroll taxes about $1 million.

In 1995, taxes (other than income taxes) were $5.4 million higher than in 1994 mostly due to higher property taxes resulting from more utility plant in service.

Other Income and Expenses

Allowance for Funds Used During Construction (AFC)
AFC is an accounting procedure used to exclude the cost of capital from expense and include it as part of the cost of utility plant construction. AFC is calculated at a rate authorized by the Maryland Commission. We describe AFC further in Note 1 on page 40.

In 1996 and 1995, we had lower AFC compared to prior years because we completed several projects and started less new construction. In 1996, we also had lower AFC because the Maryland Commission decreased the gas AFC rate in November 1995 from 9.40% to 9.04%. This meant we were not authorized to record as much gas AFC in 1996 as we were in 1995 and 1994.

Net Other Income and Deductions
Net other income and deductions represent miscellaneous income and expenses which are not directly related to operations.

In 1996, net other income and deductions increased $4.9 million compared to 1995 mostly because the Constellation Companies had lower deductions not directly related to operations and BGE had about $2 million more of other interest and finance charge income.

In 1995, net other income and deductions decreased $16.2 million compared to 1994 because we had about $12 million less of other interest and finance charge income, and we had about $4 million lower income from the sale of receivables (money customers owe to us) and property. We sell receivables to a financial institution under agreements which are discussed in Note 12 on page 48.

Interest Charges
Interest charges represent the interest we paid on outstanding debt.

In 1996, we had $2.1 million lower interest charges compared to 1995 largely because of lower interest rates. We would have had even lower interest charges except we had more debt outstanding.

In 1995, we had $5.3 million higher interest charges compared to 1994 because we had more debt outstanding and short-term interest rates were higher.

Income Taxes
In 1996 our income taxes decreased because we had lower taxable income from utility operations. Our income taxes would have been even lower except that we had higher taxable income from our diversified businesses.

In 1995, our income taxes increased because we had higher taxable income from both our utility operations and our diversified businesses.

Environmental Matters

We are subject to increasingly stringent federal, state, and local laws and regulations that work to improve or maintain the quality of the environment. If certain substances were disposed of or released at any of our properties, whether currently operating or not, these laws and regulations require us to remove or remedy the effect on the environment. This includes Environmental Protection Agency Superfund sites. You will find details of our environmental matters in Note 12 on page 49 and in our Annual Reports on Form 10-K under Item 1. Business - Environmental Matters. These details include financial information. Some of the information is about costs that may be material.

Diversified Businesses

In the 1980s, we began to diversify our business in response to limited growth in gas and electric sales. Today, we continue to diversify our business in response to regulatory changes in the utility industry. Some of our diversified businesses are related to our core utility business and others are not. Our diversified businesses include:

- Constellation Holdings, Inc. and Subsidiaries, together known as the Constellation Companies
- BGE Home Products & Services, Inc. and Subsidiary
- BGE Energy Projects & Services, Inc. and Subsidiaries
- Constellation Energy Source, Inc. (formerly named BNG, Inc.)

Diversified Business Earnings Per Share of Common Stock

	1996	1995	1994
Constellation Companies	$ .29	$ .18	$ .09
BGE Home Products & Services	.02	.00	.03
BGE Energy Projects & Services	.00	.00	–
Constellation Energy Source	.00	.00	.00
Total diversified business earnings per share	$ .31	$ .18	$ .12

Our 1996 diversified business earnings increased $19.3 million, or $.13 per share, from 1995. Our 1995 diversified business earnings increased $8.2 million, or $.06 per share, from 1994. These increases mostly reflect higher earnings from the Constellation Companies.

We discuss factors affecting the earnings of each diversified business subsidiary below.

Constellation Companies' Operations

The Constellation Companies engage in the following:

- development, ownership, and operation of power generation projects,
- financial investments, and
- development, ownership, and management of real estate and senior-living facilities.

Earnings per share from the Constellation Companies were:

	1996	1995	1994
Power generation	$ .18	$ .13	$ .10
Financial investments	.14	.08	.03
Real estate development and senior-living facilities	(.02)	(.02)	(.03)
Other	(.01)	(.01)	(.01)
Total Constellation Companies' earnings per share	$ .29	$ .18	$ .09

Power Generation

The Constellation Companies' power generation business develops, owns, and operates power generation facilities.

In 1996, earnings increased from 1995 mostly due to our share of higher earnings from energy projects and a $14.6 million after-tax gain on the sale by a Constellation partnership of a power purchase agreement with Jersey Central Power & Light Company back to that utility. Energy projects had higher earnings for a variety of reasons—some ongoing (like improved efficiency due to equipment or procedure changes) and some onetime (for example, losses incurred in 1995—to shut-down certain operations at a plant—did not occur again in 1996).

These increases were offset by:

- a $7.0 million after-tax write-off of Constellation's investment in two geothermal wholesale power generating projects,
- a $3.0 million after-tax write-off of development costs for a proposed coal-fired power project that will not be built, and
- a $6.2 million after-tax write-off of a portion of an investment in a solar power project, in which Constellation has a minority ownership interest, expected to be restructured with the lender.

In 1995, earnings increased from 1994 mostly due to our share of higher earnings from energy projects and a profit made on the sale of some operating and maintenance contracts.

California Power Purchase Agreements

The Constellation Companies have $227 million invested in 16 projects that sell electricity in California under power purchase agreements called "Interim Standard Offer No. 4" agreements.

Under these agreements, the projects supply electricity to utility companies at:

- a fixed rate for capacity and energy the first 10 years of the agreements, and
- a fixed rate for capacity plus a variable rate for energy based on the utilities' avoided cost for the remaining term of the agreements.

Generally, a "capacity rate" is paid to a power plant for its availability to supply electricity, and an "energy rate" is paid for the electricity actually generated. "Avoided cost" generally is the cost of a utility's cheapest next-available source of generation to service the demands on its system.

From 1996 through 2000, the 10-year periods for fixed energy rates expire for these 16 power generation projects and they begin supplying electricity at variable rates. When this happens, the revenues at these projects are expected to be lower than they are now. It is difficult to estimate how much lower the revenues may be, but the Constellation Companies' earnings could be affected significantly.

Eight projects begin supplying electricity at variable rates in 1997 and 1998. This means the Constellation Companies could experience lower earnings from those projects. However, the remaining projects, which will continue to supply electricity at fixed rates, are expected to have higher revenues in 1997 and 1998. These higher revenues may offset the lower revenues from the variable-rate projects during those years.

The California projects that make the highest revenues will begin supplying electricity at variable rates in 1999 and 2000. As a result, we do not expect the Constellation Companies to have significantly lower earnings due to the switch from fixed to variable rates before 2000.

In the second quarter of 1996, Constellation determined that its investments in two of these plants are not expected to be fully recoverable. Accordingly, as mentioned earlier in this section, the Constellation Companies recorded a $7.0 million after-tax write-off of the investment in these plants.

Constellation is pursuing alternatives for some of these power generation projects including:

- repowering the projects to reduce operating costs,
- changing fuels to reduce operating costs,
- renegotiating the power purchase agreements to improve the terms,
- restructuring financings to improve the financing terms, and
- selling its ownership interests in the projects.

We cannot predict the financial effects of the switch from fixed to variable rates on the Constellation Companies or on BGE, but the effects could be material.

International
Historically, Constellation's power generation projects have been in the United States. Over the last two years, however, Constellation has sought projects in Latin America. As of December 31, 1996, Constellation had invested about $17.1 million and committed another $6.5 million in power projects in Latin America. In the future, Constellation's power generation business may be expanding further in both domestic and international projects.

Financial Investments

Earnings from Constellation's portfolio of financial investments include:

- income from marketable securities,
- income from financial limited partnerships, and
- income from financial guaranty insurance companies.

In 1996, earnings were higher than in 1995 because of better earnings from marketable securities and increased gains from financial limited partnerships. In 1995, earnings were higher compared to 1994 due to: increased earnings from marketable securities, increased gains from financial limited partnerships, and higher earnings from financial guaranty insurance companies.

Real Estate Development and Senior-Living Facilities

Constellation's real estate development business includes:

- land under development,
- office buildings,
- retail projects,
- distribution facility projects,
- an entertainment, dining, and retail complex in Orlando, Florida,
- a mixed-use planned-unit development, and
- senior-living facilities.

Most of these projects are in the Baltimore-Washington corridor. The area has had a surplus of available land and office space in recent years, during a time of low economic growth and corporate downsizings. Our projects have been economically hurt by these conditions. Earnings from real estate development and senior-living facilities in 1996 and 1995 were essentially unchanged from prior years.

Constellation's real estate portfolio has continued to incur carrying costs and depreciation over the years. Additionally, the Constellation Companies have been charging interest payments to expense rather than capitalizing them for some undeveloped land where development activities have stopped. These carrying costs, depreciation, and interest expenses have decreased earnings and are expected to continue to do so.

Cash flow from real estate operations has not been enough to make the monthly loan payments on some of these projects. Cash shortfalls have been covered by cash from Constellation Holdings. Constellation Holdings obtained those funds from the cash flow from other Constellation Companies and through additional borrowing.

We will consider market demand, interest rates, the availability of financing, and the strength of the economy in general when making decisions about our real estate investments. We believe that until the economy shows sustained growth and there is more demand for new development, our real estate values will not improve much. If we were to sell our real estate projects in the current market, we would have losses, although the amount of the losses is hard to predict. Management's current real estate strategy is to hold each real estate project until we can realize a reasonable value for it. Management evaluates strategies for all its businesses, including real estate, on an ongoing basis. We anticipate that competing demands for our financial resources, changes in the utility industry, and the proposed merger with Potomac Electric Power Company, will cause us to evaluate thoroughly all diversified business strategies on a regular basis so we use capital and other resources in a manner that is most beneficial. Depending on market conditions in the future, we could also have losses on any future sales.

It may be helpful for you to understand when we are required, by accounting rules, to writedown the value of a real estate investment to market value. A writedown is required in either of two cases. The first is if we change our intent about a project from an intent to hold to an intent to sell and the market value of that project is below book value. The second is if the expected cash flow from the project is less than the investment in the project.

BGE Home Products & Services' Operations

BGE Home Products & Services engages in:

- sales and service of electric and gas appliances,
- home improvements, and
- sales and service of heating and air conditioning systems.

In 1996, earnings increased due to improved performance in the service and installation business. In 1995, earnings decreased compared to 1994 largely due to lower income from the sale of receivables during 1995. We sell receivables to a financial institution under agreements which are discussed in Note 12 on page 48.

BGE Energy Projects & Services' Operations

BGE Energy Projects & Services provides a broad range of customized energy services, including:

- power quality services,
- customer electrical system improvements,
- lighting and mechanical engineering and installation services,
- campus and multi-building energy systems,
- energy consulting and financial contracts,
- district energy systems through Comfort Link (a partnership with the Poole and Kent Company), and
- private electric and gas distribution systems.

This subsidiary was formed in November 1995. It had no significant earnings in 1996 or 1995.

Constellation Energy Source's Operations

Constellation Energy Source (formerly named BNG, Inc.) engages in natural gas brokering. This subsidiary had no significant earnings in 1996 or 1995.

Liquidity and Capital Resources

Overview

Our business requires a great deal of capital. Our actual capital requirements for the years 1994 through 1996, along with estimated amounts for the years 1997 through 1999, are shown below.

	1994	1995	1996	1997	1998	1999
Utility Business Capital Requirements:			*(In millions)*			
Construction expenditures (excluding AFC)						
Electric	$345	$223	$219	$230	$216	$ 215
Gas	68	70	84	72	70	73
Common	42	51	46	33	39	37
Total construction expenditures	455	344	349	335	325	325
AFC	34	22	10	7	7	7
Nuclear fuel (uranium purchases and processing charges)	42	46	47	49	50	50
Deferred energy conservation expenditures	41	46	31	24	19	18
Deferred nuclear expenditures	8	—	—	—	—	—
Retirement of long-term debt and redemption of preference stock	203	279	184	173	117	270
Total utility business capital requirements	783	737	621	588	518	670
Diversified Business Capital Requirements:						
Investment requirements	51	118	118	214	180	205
Retirement of long-term debt	37	55	52	108	165	186
Total diversified business capital requirements	88	173	170	322	345	391
Total capital requirements	$871	$910	$791	$910	$863	$1,061

Capital Requirements of Our Utility Business

Capital requirements for our utility business do not include costs to complete the pending merger with Potomac Electric Power Company. These costs, currently estimated to be $150 million, are discussed in more detail in Note 12 on page 48.

We continuously review and change our construction program, so actual expenditures may vary from the estimates for the years 1997 through 1999 in the capital requirements chart. Additionally, actual capital requirements may be different than the estimates for 1997 through 1999 because adjustments which may result from the pending merger with Potomac Electric Power Company have not been considered in those estimates.

Electric construction expenditures include:

- installation of a 5,000 kilowatt diesel generator which was placed in service in 1996 at our Calvert Cliffs Nuclear Power Plant, and
- improvements to other generating plants and to our transmission and distribution facilities.

Our projections of future electric construction expenditures do not include costs to build more generating units.

Our utility operations provided about 96% in 1996, 100% in 1995, and 72% in 1994, of the cash needed to meet our capital requirements, excluding cash needed to retire debt and redeem preferred and preference stock. In addition, in 1994, the sale of some receivables provided $70 million in cash. This is discussed in more detail in Note 12 on page 48.

During the three years from 1997 through 1999, we expect utility operations to provide 115% of the cash needed to meet our capital requirements, excluding cash needed to retire debt and redeem preference stock. This estimate does not consider the pending merger with Potomac Electric Power Company.

When we cannot meet utility capital requirements internally, we sell debt and equity securities. The amount of cash we need and market conditions determine when and how much we sell. During the three years ended December 31, 1996, we sold:

- $540 million of long-term debt,
- $60 million of preference stock, and
- $39 million of common stock.

Security Ratings

Independent credit-rating agencies rate our fixed-income securities. The ratings indicate the agencies' assessment of our ability to pay interest, dividends, and principal on these securities. These ratings affect how much it will cost us to sell these securities. The better the rating, the cheaper it is for us to sell. At the date of this report, our securities ratings were as follows:

	Standard & Poors Rating Group	Moody's Investors Service	Duff & Phelps Credit Rating Co.
Mortgage Bonds	A+	A1	AA–
Unsecured Debt	A	A2	A+
Preference Stock	A	"a2"	A

Capital Requirements of Our Diversified Businesses

In the past, capital requirements of our diversified businesses only included the Constellation Companies because they had the only significant capital requirements. From time to time, however, our other diversified businesses may develop significant capital requirements. As that occurs, we will include the capital requirements of those businesses in the capital requirements table on page 28. As discussed below under "Investment Requirements," capital requirements for Comfort Link are also included this year.

Our Constellation Companies and other diversified businesses expect to expand their businesses. This will include our new power marketing business. It also may include expansion in the energy, financial investments, real estate, and senior-living facility businesses. Such expansion could mean more investments in and acquisition of new projects. Our Constellation Companies and other diversified businesses have met their capital requirements in the past through borrowing, cash from their operations, and from time to time, loans or equity contributions from BGE. Our Constellation Companies and other diversified businesses plan to raise the cash needed to meet capital requirements in the future through these same methods.

Investment Requirements

The investment requirements of our diversified businesses include:

- for the Constellation Companies, investments in financial limited partnerships and funding for the development and acquisition of projects, as well as loans made to project partnerships, and
- for BGE Energy Projects & Services, funding for construction of district energy projects of Comfort Link.

Investment requirements for 1997 through 1999 include estimates of funding for existing and new projects and for our new power marketing business. We continuously review and modify those estimates. Actual investment requirements could vary a great deal from the estimates on page 28 because they would be subject to several variables, including:

- the type and number of projects selected for development,
- the effect of market conditions on those projects,
- opportunities for growth in the power marketing business,
- the ability to obtain financing, and
- the availability of cash from operations.

Debt and Liquidity

Our diversified businesses plan to meet capital requirements by refinancing debt as it comes due, by additional borrowing, and with cash generated by the businesses. This includes cash from operations, sale of assets, and earned tax benefits. BGE Home Products & Services may also meet capital requirements through sales of receivables as discussed in Note 12 on page 48.

If Constellation can get a reasonable value for its real estate, it could obtain additional cash by selling real estate projects. For more information, see the discussion of the real estate business and market on page 27. Constellation's ability to sell or liquidate assets will depend on market conditions, and we cannot give assurances that these sales or liquidations could be made.

In addition, Constellation has a $75 million revolving credit agreement and Comfort Link has a $50 million revolving credit agreement to provide additional cash for short-term financial needs.

Report of Management

The management of the Company is responsible for the information and representations in the Company's financial statements. The Company prepares the financial statements in accordance with generally accepted accounting principles based upon available facts and circumstances and management's best estimates and judgments of known conditions.

The Company maintains an accounting system and related system of internal controls designed to provide reasonable assurance that the financial records are accurate and that the Company's assets are protected. The Company's staff of internal auditors, which reports directly to the Chairman of the Board, conducts periodic reviews to maintain the effectiveness of internal control procedures. Coopers & Lybrand L.L.P., independent accountants, audit the financial statements and express their opinion about them. They perform their audit in accordance with generally accepted auditing standards.

The Audit Committee of the Board of Directors, which consists of four outside Directors, meets periodically with Management, internal auditors, and Coopers & Lybrand L.L.P. to review the activities of each in discharging their responsibilities. The internal audit staff and Coopers & Lybrand L.L.P. have free access to the Audit Committee.

Christian H. Poindexter
Chairman of the Board
and Chief Executive Officer

Charles W. Shivery
Chief Financial Officer

Report of Independent Accountants

To the Shareholders of
Baltimore Gas and Electric Company

We have audited the accompanying consolidated balance sheets and statements of capitalization of Baltimore Gas and Electric Company and Subsidiaries as of December 31, 1996 and 1995, and the related consolidated statements of income, cash flows, common shareholders' equity, and income taxes for each of the three years in the period ended December 31, 1996. These financial statements are the responsibility of the Company's Management. Our responsibility is to express an opinion on these financial statements based on our audits.

We conducted our audits in accordance with generally accepted auditing standards. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by Management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, the financial statements referred to above present fairly, in all material respects, the consolidated financial position of Baltimore Gas and Electric Company and Subsidiaries as of December 31, 1996 and 1995, and the consolidated results of their operations and their cash flows for each of the three years in the period ended December 31, 1996 in conformity with generally accepted accounting principles.

Coopers & Lybrand L.L.P.

Coopers & Lybrand L.L.P.
Baltimore, Maryland
January 17, 1997

Consolidated Statements of Income

Year Ended December 31,	1996	1995	1994
		(In thousands, except per share amounts)	
Revenues			
Electric	$2,208,744	$2,229,774	$2,126,581
Gas	517,292	400,504	421,249
Diversified businesses	427,211	304,521	235,155
Total revenues	3,153,247	2,934,799	2,782,985
Expenses Other Than Interest and Income Taxes			
Electric fuel and purchased energy	547,414	578,801	542,314
Disallowed replacement energy costs (see Note 12)	95,369	—	—
Gas purchased for resale	284,443	198,069	224,590
Operations	526,424	550,811	552,817
Maintenance	174,141	168,269	164,892
Diversified businesses - selling, general, and administrative	311,053	220,573	167,430
Depreciation and amortization	330,191	317,417	295,950
Taxes other than income taxes	214,747	205,167	199,733
Total expenses other than interest and income taxes	2,483,782	2,239,107	2,147,726
Income from Operations	669,465	695,692	635,259
Other Income			
Allowance for equity funds used during construction	6,508	14,162	21,746
Equity in earnings of Safe Harbor Water Power Corporation	4,596	4,559	4,349
Net other income and (deductions)	(4,974)	(9,902)	6,270
Total other income	6,130	8,819	32,365
Income Before Interest and Income Taxes	675,595	704,511	667,624
Interest Expense			
Interest charges	217,622	219,689	214,347
Capitalized interest	(15,664)	(15,050)	(12,427)
Allowance for borrowed funds used during construction	(3,520)	(7,662)	(11,766)
Net interest expense	198,438	196,977	190,154
Income Before Income Taxes	477,157	507,534	477,470
Income Taxes	166,333	169,527	153,853
Net Income	310,824	338,007	323,617
Preferred and Preference Stock Dividends	38,536	40,578	39,922
Earnings Applicable to Common Stock	$ 272,288	$ 297,429	$ 283,695
Average Shares of Common Stock Outstanding	147,560	147,527	147,100
Earnings Per Share of Common Stock	$1.85	$2.02	$1.93

See Notes to Consolidated Financial Statements.

Consolidated Balance Sheets

At December 31,	1996	1995
	(In thousands)	
Assets		
Current Assets		
Cash and cash equivalents	$ 66,708	$ 23,443
Accounts receivable (net of allowance for uncollectibles of $18,028 and $16,390, respectively)	419,479	400,005
Trading securities	68,794	47,990
Fuel stocks	87,073	59,614
Materials and supplies	147,729	145,900
Prepaid taxes other than income taxes	64,763	60,508
Deferred income taxes	2,943	36,831
Other	44,709	31,487
Total current assets	902,198	805,778
Investments and Other Assets		
Real estate projects	525,765	479,344
Power generation projects	379,130	358,629
Financial investments	204,443	205,841
Nuclear decommissioning trust fund	116,368	85,811
Net pension asset	84,510	60,077
Safe Harbor Water Power Corporation	34,363	34,327
Senior living facilities	36,415	16,045
Other	92,171	71,894
Total investments and other assets	1,473,165	1,311,968
Utility Plant		
Plant in service		
Electric	6,514,950	6,360,624
Gas	776,973	692,693
Common	523,485	522,450
Total plant in service	7,815,408	7,575,767
Accumulated depreciation	(2,613,355)	(2,481,801)
Net plant in service	5,202,053	5,093,966
Construction work in progress	221,857	247,296
Nuclear fuel (net of amortization)	132,937	130,782
Plant held for future use	25,503	25,552
Net utility plant	5,582,350	5,497,596
Deferred Charges		
Regulatory assets (net)	512,279	637,915
Other	80,978	63,406
Total deferred charges	593,257	701,321
Total Assets	$8,550,970	$8,316,663

See Notes to Consolidated Financial Statements.

Consolidated Balance Sheets

At December 31,	1996	1995
	(In thousands)	
Liabilities and Capitalization		
Current Liabilities		
Short-term borrowings	$ 333,185	$ 279,305
Current portions of long-term debt and preference stock	280,772	146,969
Accounts payable	172,889	177,092
Customer deposits	27,993	26,857
Accrued taxes	6,473	8,244
Accrued interest	57,440	56,670
Dividends declared	66,950	67,198
Accrued vacation costs	34,351	33,403
Other	37,046	39,417
Total current liabilities	1,017,099	835,155
Deferred Credits and Other Liabilities		
Deferred income taxes	1,300,174	1,311,530
Postretirement and postemployment benefits	169,253	148,594
Decommissioning of federal uranium enrichment facilities	38,599	43,695
Other	65,463	55,568
Total deferred credits and other liabilities	1,573,489	1,559,387
Capitalization		
Long-term debt	2,758,769	2,598,254
Preferred stock	—	59,185
Redeemable preference stock	134,500	242,000
Preference stock not subject to mandatory redemption	210,000	210,000
Common shareholders' equity	2,857,113	2,812,682
Total capitalization	5,960,382	5,922,121
Commitments, Guarantees, and Contingencies – See Note 12		
Total Liabilities and Capitalization	$8,550,970	$8,316,663

See Notes to Consolidated Financial Statements.

Consolidated Statements of Cash Flows

Year Ended December 31,	1996	1995	1994
		(In thousands)	
Cash Flows From Operating Activities			
Net income	**$310,824**	$338,007	$323,617
Adjustments to reconcile to net cash provided by operating activities			
Depreciation and amortization	**383,155**	378,977	351,064
Deferred income taxes	**26,009**	103,494	79,278
Investment tax credit adjustments	**(7,655)**	(8,088)	(8,192)
Deferred fuel costs	**528**	5,565	11,461
Deferred energy conservation revenues	**28,509**	1,283	18,769
Disallowed replacement energy costs	**95,369**	—	—
Accrued pension and postemployment benefits	**(13,792)**	(7,641)	(41,113)
Allowance for equity funds used during construction	**(6,508)**	(14,162)	(21,746)
Equity in earnings of affiliates and joint ventures (net)	**(48,305)**	(21,259)	(20,225)
Changes in current assets other than sale of accounts receivable	**(88,035)**	(107,392)	(10,536)
Changes in current liabilities, other than short-term borrowings	**(4,905)**	(7,293)	(24,447)
Other	**26,762**	6,661	(5,699)
Net cash provided by operating activities	**701,947**	668,152	652,231
Cash Flows From Financing Activities			
Proceeds from issuance of			
Short-term borrowings (net)	**53,880**	215,605	63,700
Long-term debt	**383,182**	184,422	207,169
Preference stock	**—**	59,329	—
Common stock	**3,729**	318	33,869
Proceeds from sale of receivables	**10,000**	2,000	70,000
Reacquisition of long-term debt	**(158,551)**	(315,105)	(240,853)
Reacquisition of preferred and preference stock	**(112,559)**	(73,000)	(4,406)
Common stock dividends paid	**(233,109)**	(227,192)	(220,152)
Preferred and preference stock dividends paid	**(37,950)**	(40,087)	(39,950)
Other	**(1,172)**	13	(437)
Net cash used in financing activities	**(91,650)**	(193,697)	(131,060)
Cash Flows From Investing Activities			
Utility construction expenditures (including AFC)	**(360,485)**	(366,037)	(488,976)
Allowance for equity funds used during construction	**6,508**	14,162	21,746
Nuclear fuel expenditures	**(46,761)**	(46,330)	(42,089)
Deferred nuclear expenditures	**—**	—	(8,393)
Deferred energy conservation expenditures	**(31,383)**	(45,503)	(40,440)
Contributions to nuclear decommissioning trust fund	**(25,483)**	(9,780)	(9,780)
Purchases of marketable equity securities	**(32,664)**	(18,447)	(52,099)
Sales of marketable equity securities	**39,657**	49,788	40,585
Other financial investments	**7,068**	9,423	2,469
Real estate projects	**(55,344)**	(15,599)	14,926
Power generation systems	**(5,332)**	(34,408)	(1,116)
Other	**(62,813)**	(26,871)	(3,650)
Net cash used in investing activities	**(567,032)**	(489,602)	(566,817)
Net Increase (Decrease) in Cash and Cash Equivalents	**43,265**	(15,147)	(45,646)
Cash and Cash Equivalents at Beginning of Year	**23,443**	38,590	84,236
Cash and Cash Equivalents at End of Year	**$ 66,708**	$ 23,443	$ 38,590
Other Cash Flow Information			
Cash paid during the year for:			
Interest (net of amounts capitalized)	**$182,431**	$195,308	$184,441
Income taxes	**$160,132**	$ 99,623	$ 83,143

See Notes to Consolidated Financial Statements.

Certain prior-year amounts have been reclassified to conform with the current year's presentation.

Consolidated Statements of Common Shareholders' Equity

Years Ended December 31, 1996, 1995, and 1994	Common Stock Shares	Common Stock Amount	Retained Earnings	Unrealized Gain (Loss) on Available For Sale Securities	Pension Liability Adjustment	Total Amount
			(In thousands)			
Balance at December 31, 1993	146,034	$1,391,464	$1,251,140	$ —	$(22,093)	$2,620,511
Net income			323,617			323,617
Dividends declared						
Preferred and preference stock			(39,922)			(39,922)
Common stock ($1.51 per share)			(222,180)			(222,180)
Common stock issued	1,493	33,869				33,869
Other		45				45
Net unrealized loss on securities				(5,609)		(5,609)
Deferred taxes on net unrealized loss on securities				1,963		1,963
Pension liability adjustment					8,573	8,573
Deferred taxes on pension liability adjustment					(3,001)	(3,001)
Balance at December 31, 1994	147,527	1,425,378	1,312,655	(3,646)	(16,521)	2,717,866
Net income			338,007			338,007
Dividends declared						
Preferred and preference stock			(40,578)			(40,578)
Common stock ($1.55 per share)			(228,667)			(228,667)
Common stock issued		318				318
Other		109				109
Net unrealized gain on securities				14,010		14,010
Deferred taxes on net unrealized gain on securities				(4,904)		(4,904)
Pension liability adjustment					25,417	25,417
Deferred taxes on pension liability adjustment					(8,896)	(8,896)
Balance at December 31, 1995	147,527	1,425,805	1,381,417	5,460	—	2,812,682
Net income			**310,824**			**310,824**
Dividends declared						
Preferred and preference stock			**(38,536)**			**(38,536)**
Common stock ($1.59 per share)			**(234,640)**			**(234,640)**
Common stock issued	**140**	**3,729**				**3,729**
Other		**408**				**408**
Net unrealized gain on securities				**4,071**		**4,071**
Deferred taxes on net unrealized gain on securities				**(1,425)**		**(1,425)**
Balance at December 31, 1996	**147,667**	**$1,429,942**	**$1,419,065**	**$8,106**	**$ —**	**$2,857,113**

See Notes to Consolidated Financial Statements.

Consolidated Statements of Capitalization

At December 31,	1996	1995
	(In thousands)	
Long-Term Debt		
First Refunding Mortgage Bonds of BGE		
5⅛% Series, due April 15, 1996	$ —	$ 26,187
6⅛% Series, due August 1, 1997	24,935	24,935
Floating rate series, due April 15, 1999	125,000	125,000
8.40% Series, due October 15, 1999	91,137	91,200
5½% Series, due July 15, 2000	124,990	125,000
8⅛% Series, due August 15, 2001	122,377	122,427
7⅛% Series, due January 1, 2002	22,737	39,698
7⅛% Series, due July 1, 2002	124,484	124,609
5½% Installment Series, due July 15, 2002	10,440	11,045
6½% Series, due February 15, 2003	124,822	124,882
6⅛% Series, due July 1, 2003	124,855	124,925
5½% Series, due April 15, 2004	124,995	124,995
Remarketed floating rate series, due September 1, 2006	125,000	—
7½% Series, due January 15, 2007	123,652	123,667
6⅛% Series, due March 15, 2008	124,960	124,985
7½% Series, due March 1, 2023	124,973	124,973
7½% Series, due April 15, 2023	100,000	100,000
Total First Refunding Mortgage Bonds of BGE	1,619,357	1,538,528
Other long-term debt of BGE		
Term bank loan due March 29, 2001	50,000	50,000
Medium-term notes, Series A	—	10,500
Medium-term notes, Series B	100,000	100,000
Medium-term notes, Series C	183,000	200,000
Medium-term notes, Series D	138,000	28,000
Pollution control loan, due July 1, 2011	36,000	36,000
Port facilities loan, due June 1, 2013	48,000	48,000
Adjustable rate pollution control loan, due July 1, 2014	20,000	20,000
5.55% Pollution control revenue refunding loan, due July 15, 2014	47,000	47,000
Economic development loan, due December 1, 2018	35,000	35,000
6.00% Pollution control revenue refunding loan, due April 1, 2024	75,000	75,000
Total other long-term debt of BGE	732,000	649,500
Long-term debt of Constellation Companies		
Revolving credit agreement		
Variable rates based on LIBOR, due December 9, 1999	65,000	1,000
Mortgage and construction loans and other collateralized notes		
8.00%, due July 31, 2001	141	—
8.00%, due October 30, 2003	1,500	—
Variable rates, due through 2009	128,571	110,018
7.50%, due October 9, 2005	9,846	9,989
7.357%, due March 15, 2009	5,763	5,896
9.65%, due February 1, 2028	9,746	—
Unsecured notes	387,160	420,000
Total long-term debt of Constellation Companies	607,727	546,903
Long-term debt of other diversified businesses		
Loans under revolving credit agreements	12,000	—
Unamortized discount and premium	(14,543)	(15,708)
Current portion of long-term debt	(197,772)	(120,969)
Total long-term debt	$2,758,769	$2,598,254

continued on page 37

See Notes to Consolidated Financial Statements.

Consolidated Statements of Capitalization

At December 31,	**1996**	1995
	(In thousands)	
Preferred Stock		
Cumulative, $100 par value, 1,000,000 shares authorized		
Series B, 4½%, 222,921 shares redeemed at $110 per share on May 28, 1996	$ —	$ 22,292
Series C, 4%, 68,928 shares redeemed at $105 per share on May 28, 1996	—	6,893
Series D, 5.40%, 300,000 shares redeemed at $101 per share on May 28, 1996	—	30,000
Total preferred stock	—	59,185
Preference Stock		
Cumulative, $100 par value, 6,500,000 shares authorized		
Redeemable preference stock		
7.50%, 1986 Series, 395,000 and 425,000 shares outstanding. Callable at $102.50 per share prior to October 1, 2001 and at lesser amounts thereafter	39,500	42,500
6.75%, 1987 Series, 440,000 and 455,000 shares outstanding. Callable at $104.50 per share prior to April 1, 1997 and at lesser amounts thereafter	44,000	45,500
7.80%, 1989 Series, 500,000 shares outstanding	50,000	50,000
8.25%, 1989 Series, 100,000 and 300,000 shares outstanding	10,000	30,000
8.625%, 1990 Series, 390,000 and 650,000 shares outstanding	39,000	65,000
7.85%, 1991 Series, 350,000 shares outstanding	35,000	35,000
Current portion of redeemable preference stock	(83,000)	(26,000)
Total redeemable preference stock	134,500	242,000
Preference stock not subject to mandatory redemption		
7.78%, 1973 Series, 200,000 shares outstanding, callable at $101 per share	20,000	20,000
7.125%, 1993 Series, 400,000 shares outstanding, not callable prior to July 1, 2003	40,000	40,000
6.97%, 1993 Series, 500,000 shares outstanding, not callable prior to October 1, 2003	50,000	50,000
6.70%, 1993 Series, 400,000 shares outstanding, not callable prior to January 1, 2004	40,000	40,000
6.99%, 1995 Series, 600,000 shares outstanding, not callable prior to October 1, 2005	60,000	60,000
Total preference stock not subject to mandatory redemption	210,000	210,000
Common Shareholders' Equity		
Common stock without par value, 175,000,000 shares authorized; 147,667,114 and 147,527,114 shares issued and outstanding at December 31, 1996 and 1995, respectively. (At December 31, 1996, 166,893 shares were reserved for the Employee Savings Plan and 3,277,656 shares were reserved for the Dividend Reinvestment and Stock Purchase Plan.)	1,429,942	1,425,805
Retained earnings	1,419,065	1,381,417
Unrealized gain (loss) on available-for-sale securities	8,106	5,460
Total common shareholders' equity	2,857,113	2,812,682
Total Capitalization	$5,960,382	$5,922,121

See Notes to Consolidated Financial Statements.

Consolidated Statements of Income Taxes

Year Ended December 31,	1996	1995	1994
		(Dollar amounts in thousands)	
Income Taxes			
Current	$147,979	$ 74,121	$ 82,767
Deferred			
Change in tax effect of temporary differences	22,516	118,300	88,896
Change in income taxes recoverable through future rates	4,918	(1,006)	(8,580)
Deferred taxes credited (charged) to shareholders' equity	(1,425)	(13,800)	(1,038)
Deferred taxes charged to expense	26,009	103,494	79,278
Investment tax credit adjustments	(7,655)	(8,088)	(8,192)
Income taxes per Consolidated Statements of Income	$166,333	$169,527	$153,853
Reconciliation of Income Taxes Computed at Statutory Federal Rate to Total Income Taxes			
Income before income taxes	$477,157	$507,534	$477,470
Statutory federal income tax rate	35%	35%	35%
Income taxes computed at statutory federal rate	167,005	177,637	167,115
Increases (decreases) in income taxes due to			
Depreciation differences not normalized on regulated activities	12,669	10,953	9,791
Allowance for equity funds used during construction	(2,278)	(4,957)	(7,611)
Amortization of deferred investment tax credits	(7,655)	(8,088)	(8,164)
Tax credits flowed through to income	(520)	(521)	(1,754)
Amortization of deferred tax rate differential on regulated activities	(1,958)	(2,013)	(1,885)
Other	(930)	(3,484)	(3,639)
Total income taxes	$166,333	$169,527	$153,853
Effective federal income tax rate	34.9%	33.4%	32.2%

At December 31,	1996	1995
Deferred Income Taxes	*(Dollar amounts in thousands)*	
Deferred tax liabilities		
Accelerated depreciation	$ 920,631	$ 878,470
Allowance for funds used during construction	209,183	210,928
Income taxes recoverable through future rates	92,584	94,305
Deferred termination and postemployment costs	45,624	49,591
Deferred fuel costs	7,957	39,559
Leveraged leases	27,581	29,842
Percentage repair allowance	38,354	38,295
Energy conservation expenditures	26,622	28,121
Other	175,587	151,231
Total deferred tax liabilities	1,544,123	1,520,342
Deferred tax assets		
Alternative minimum tax	—	32,626
Accrued pension and postemployment benefit costs	40,570	31,707
Deferred investment tax credits	46,889	49,512
Capitalized interest and overhead	42,509	39,439
Contributions in aid of construction	35,710	34,404
Nuclear decommissioning liability	18,750	16,708
Other	62,464	41,247
Total deferred tax assets	246,892	245,643
Deferred tax liability, net	$1,297,231	$1,274,699

See Notes to Consolidated Financial Statements.

Notes to Consolidated Financial Statements

Note 1. Significant Accounting Policies

Nature of the Business
Baltimore Gas and Electric Company (BGE) and Subsidiaries (collectively, the Company) is primarily an electric and gas utility serving a territory which encompasses Baltimore City and all or part of ten Central Maryland counties. The Company is also engaged in diversified businesses as described further in Note 3.

Principles of Consolidation
The consolidated financial statements include the accounts of BGE and all subsidiaries in which BGE owns directly or indirectly a majority of the voting stock. Intercompany balances and transactions are eliminated in consolidation. Under this policy, the accounts of Constellation Holdings, Inc. (CHI) and Subsidiaries (collectively, the Constellation Companies), BGE Home Products & Services, Inc. and Subsidiary (collectively, HP&S), BGE Energy Projects & Services, Inc. and Subsidiaries (collectively, EP&S), and Constellation Energy Source, Inc. (formerly named BNG, Inc.) are consolidated in the financial statements, and Safe Harbor Water Power Corporation is reported under the equity method. Corporate joint ventures, partnerships, and affiliated companies (which include power generation projects) in which a 20% to 50% voting interest is held are accounted for under the equity method, unless control is evident, in which case the entity is consolidated. Investments in which less than a 20% voting interest is held are accounted for under the cost method, unless significant influence is exercised over the entity, in which case the investment is accounted for under the equity method.

Regulation of Utility Operations
BGE's utility operations are subject to regulation by the Maryland Public Service Commission (Maryland Commission). The accounting policies and practices used in the determination of service rates are also generally used for financial reporting purposes in accordance with generally accepted accounting principles for regulated industries. See Note 5.

Utility Revenues
BGE recognizes utility revenues as service is rendered to customers.

Fuel and Purchased Energy Costs
The cost of fuel used in generating electricity, net of revenues from interchange sales, is recovered through a zero-based electric fuel rate subject to approval by the Maryland Commission. The difference between actual fuel costs and fuel revenues is deferred on the Consolidated Balance Sheets to be recovered from or refunded to customers in future periods. The electric fuel rate formula is based upon the latest twenty-four-month generation mix and the latest three-month average fuel cost for each generating unit. The fuel rate does not change unless the calculated rate is more than 5% above or below the rate then in effect.

During 1989 through 1991 BGE experienced extended outages at its Calvert Cliffs Nuclear Power Plant. The replacement energy costs associated with these outages are estimated to be $458 million. The extended outages have been the subject of ongoing fuel rate proceedings before the Maryland Commission for several years (see Note 12).

In December 1996, BGE entered into a settlement agreement with the Maryland People's Counsel and the Maryland Commission Staff proposing that customers will not fund a total of $118 million of electric replacement energy costs associated with these extended outages. BGE recorded a reserve for $35 million of these costs in 1990. In 1996, BGE increased the reserve by $83 million and wrote off $5.6 million of accrued carrying charges related to the deferred fuel balances. These increases in the reserve reduced 1996 after-tax earnings by $57.6 million, or 39 cents per share. In addition, the Maryland Commission issued a rate order in May 1996 disallowing certain fuel costs which were previously deferred by BGE. Accordingly, BGE wrote-off the deferred fuel costs in 1996. The write-off of these costs reduced after-tax earnings by $4.5 million, or 3 cents per share.

Prior to October 1996, the cost of gas sold was recovered through gas adjustment clauses subject to approval by the Maryland Commission. Under these clauses, the difference between actual fuel costs and fuel revenues is deferred on the balance sheet and recovered from or refunded to customers in future periods. Effective October 1996, the Maryland Commission approved a modification of these clauses to provide a Market Based Rates (MBR) incentive mechanism. Under the MBR mechanism, differences between a market index and BGE's actual cost of gas are shared equally between BGE's customers and shareholders.

Risk Management
Beginning in 1996, BGE engages in commodity hedging activities to minimize the risk of market fluctuations associated with the price of gas under the MBR mechanism. The objective of hedging is to manage BGE's price risk under the MBR mechanism. Under internal guidelines, speculative positions are prohibited.

BGE enters into basis swap agreements which help minimize commodity price risk by fixing the basis or differential that exists between a delivery location index and the commodity futures prices. Net amounts receivable or payable under the swaps are deferred and recognized as a component of gas costs when realized. At December 31, 1996, there were unsettled swap agreements representing a notional quantity of 12.3 million decatherms of natural gas purchases through March 1997.

Income Taxes
The deferred tax liability represents the tax effect of temporary differences between the financial-statement and tax bases of assets and liabilities. It is measured using presently enacted tax rates. The portion of BGE's deferred tax liability applicable to utility operations which has not been reflected in current service rates represents income taxes recoverable through future rates. That portion has been recorded as a regulatory asset on the Consolidated Balance Sheets. Deferred income tax expense represents the net change in the deferred tax liability and regulatory asset during the year, exclusive of amounts charged or credited to common shareholders' equity.

Current tax expense consists solely of regular tax less applicable tax credits. In certain prior years, tax expense included an alternative minimum tax (AMT) that can be carried forward indefinitely as tax credits to future years in which the regular tax liability exceeds the AMT liability. Current income tax for the years ended December 31, 1996 and 1995 reflect full utilization of AMT credits carried forward of $30 million and $40 million, respectively. The deferred income taxes provided in earlier years on the AMT liability were reversed as the credits were utilized.

The investment tax credit (ITC) associated with BGE's regulated utility operations has been deferred on the Consolidated Balance Sheets (see Note 5) and is amortized to income ratably over the lives of the subject property. ITC and other tax credits associated with nonregulated diversified businesses other than leveraged leases are flowed through to income.

BGE's utility revenue from system sales is subject to the Maryland public service company franchise tax in lieu of a state income tax. The franchise tax is included in taxes other than income taxes in the Consolidated Statements of Income.

Inventory Valuation
Fuel stocks and materials and supplies are generally stated at average cost.

Impairment of Long-Lived Assets
Long-lived assets subject to the requirements of Statement of Financial Accounting Standards No. 121, *Accounting for the Impairment of Long-Lived Assets and for Long-Lived Assets to Be Disposed Of*, are evaluated for impairment through a review of undiscounted expected future cash flows. If the sum of the undiscounted expected future cash flows is less than the carrying amount of the asset, an impairment loss is recognized.

Real Estate Projects
Real estate projects consist of the Constellation Companies' investments in rental and operating properties and properties under development. Rental and operating properties are held for investment. Properties under development are held for future development and subsequent sale. Costs incurred in the acquisition and active development of such properties are capitalized. Rental and operating properties and properties under development are stated at cost unless the amount invested exceeds the amounts expected to be recovered through operations and sales. In these cases, the projects are written down to the amount estimated to be recoverable.

Investments and Other Assets
Investments in debt and equity securities subject to the requirements of Statement of Financial Accounting Standards No. 115, Accounting for Certain Investments in Debt and Equity Securities, are reported at fair value. Certain of Constellation Companies' marketable equity securities and financial partnerships are classified as trading securities. Unrealized gains and losses on these securities are included in diversified businesses revenues. The investments comprising the nuclear decommissioning trust fund and certain marketable equity securities of CHI are classified as available-for-sale. Unrealized gains and losses on these securities, as well as CHI's portion of unrealized gains and losses on securities of equity-method investees, are recorded in shareholders' equity. The Company utilizes specific identification to determine the cost of these securities in computing realized gains or losses.

Utility Plant, Depreciation and Amortization, and Decommissioning
Utility plant is stated at original cost, which includes material, labor, and, where applicable, construction overhead costs and an allowance for funds used during construction. Additions to utility plant and replacements of units of property are capitalized to utility plant accounts. Utility plant retired or otherwise disposed of is charged to accumulated depreciation. Maintenance and repairs of property and replacements of items of property determined to be less than a unit of property are charged to maintenance expense.

Depreciation is generally computed using composite straight-line rates applied to the average investment in classes of depreciable property. Vehicles are depreciated based on their estimated useful lives. As a result of the Maryland Commission's November 1995 gas rate Order, BGE revised its gas utility plant depreciation rates to reflect the results of a detailed depreciation study. The revised rates resulted in an increase in depreciation accruals of approximately $2.4 million annually.

Depreciation expense for 1995 and 1994 includes the write-off of certain costs at BGE's Perryman site. Initially, BGE had planned to build two combined cycle generating units at its Perryman site with each unit consisting of two combustion turbines. However, due to significant changes in the environment in which utilities operate, BGE decided in 1994 not to construct the second combined cycle generating unit and wrote off the construction work in progress costs associated with that unit. This write-off reduced after-tax earnings during 1994 by $11.0 million or 7 cents per share. As a result of the Maryland Commission's August 1995 Order requiring all new generation capacity needs to be competitively bid and BGE's September 1995 announcement that it will merge with Potomac Electric Power Company, BGE determined that it will not build the second combustion turbine for the first combined cycle unit. Therefore, during the third quarter of 1995, BGE wrote off the remaining construction work in progress costs associated with the first combined cycle unit. This write-off reduced after-tax earnings during 1995 by $9.7 million, or 7 cents per share. The construction of the first 140-megawatt combustion turbine at Perryman was completed, and the unit was placed in service, during June 1995.

BGE owns an undivided interest in the Keystone and Conemaugh electric generating plants located in western Pennsylvania, as well as in the transmission line which transports the plants' output to the joint owners' service territories. BGE's ownership interest in these plants is 20.99% and 10.56%, respectively, and represents a net investment of $153 million and $150 million as of December 31, 1996 and 1995, respectively. Financing and accounting for these properties are the same as for wholly owned utility plant.

Nuclear fuel expenditures are amortized as a component of actual fuel costs based on the energy produced over the life of the fuel. Fees for the future disposal of spent nuclear fuel are paid quarterly to the Department of Energy and are accrued based on the kilowatt-hours of electricity sold. Nuclear fuel expenses are subject to recovery through the electric fuel rate.

Nuclear decommissioning costs are accrued by and recovered through a sinking fund methodology. In a 1995 order, the Maryland Commission authorized BGE to record decommissioning expense based on a facility-specific cost estimate in order to accumulate a decommissioning reserve of $521 million in 1993 dollars by the end of Calvert Cliffs' service life in 2016, adjusted to reflect expected inflation, to decommission the radioactive portion of the plant. The total decommissioning reserve of $163.8 million and $136.7 million at December 31, 1996 and 1995, respectively, is included in accumulated depreciation in the Consolidated Balance Sheets.

In accordance with Nuclear Regulatory Commission (NRC) regulations, BGE has established an external decommissioning trust to which a portion of accrued decommissioning costs have been contributed. The NRC requires utilities to provide financial assurance that they will accumulate sufficient funds to pay for the cost of nuclear decommissioning based upon either a generic NRC formula or a facility-specific decommissioning cost estimate. BGE is using the facility-specific cost estimate for funding these costs and providing the requisite financial assurance.

Allowance for Funds Used During Construction and Capitalized Interest
The allowance for funds used during construction (AFC) is an accounting procedure which capitalizes the cost of funds used to finance utility construction projects as part of utility plant on the Consolidated Balance Sheets, crediting the cost as a noncash item on the Consolidated Statements of Income. The cost of borrowed and equity funds is segregated between interest expense and other income, respectively. BGE recovers the capitalized AFC and a return thereon after the related utility plant is placed in service and included in depreciable assets and rate base.

Prior to November 20, 1995, the Company accrued AFC at a pre-tax rate of 9.40%. Effective November 20, 1995, a rate order of the Maryland Commission reduced the pre-tax gas-plant and common-plant AFC rates to 9.04% and 9.36%, respectively. AFC is compounded annually.

The Constellation Companies capitalize interest on qualifying real estate and power generation development projects.

Long-Term Debt
The discount or premium and expense of issuance associated with long-term debt are deferred and amortized over the original lives of the respective debt issues. Gains and losses on the reacquisition of debt are amortized over the remaining original lives of the issuances.

Cash Flows
For the purpose of reporting cash flows, highly liquid investments purchased with a maturity of three months or less are considered to be cash equivalents.

Use of Accounting Estimates
The preparation of financial statements in conformity with generally accepted accounting principles requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. These estimates involve judgments with respect to, among other things, various future economic factors which are difficult to predict and are beyond the control of the Company. Therefore, actual amounts could differ from these estimates.

Accounting Standards Issued
The Financial Accounting Standards Board has issued Statement of Financial Accounting Standards No. 125, regarding accounting for transfers and servicing of financial assets and extinguishments of liabilities, effective January 1, 1997. The American Institute of Certified Public Accountants has issued Statement of Position No. 96-1, regarding accounting for environmental remediation liabilities, effective January 1, 1997. Adoption of these statements is not expected to have a material impact on the Company's financial statements.

Note 2. Segment Information

	Nonaffiliated Revenues	Affiliated Revenues	Total Revenues	Income from Operations	Depreciation/ Amortization	Construction Expenditures (Including AFC)	Identifiable Assets at December 31
				(In thousands)			
1996							
Electric	$2,208,744	$ 283	$2,209,027	$497,986	$279,345	$262,542	$6,226,291
Gas	517,292	—	517,292	68,848	37,790	97,943	810,084
Diversified businesses	427,211	6,782	433,993	102,631	13,056	—	1,400,553
Other identifiable assets	—	—	—	—	—	—	114,042
Intercompany eliminations	—	(7,065)	(7,065)	—	—	—	—
Total	$3,153,247	$ —	$3,153,247	$669,465	$330,191	$360,485	$8,550,970
1995							
Electric	$2,229,774	$1,337	$2,231,111	$574,299	$276,285	$288,509	$6,195,722
Gas	400,504	—	400,504	48,104	29,637	77,528	748,462
Diversified businesses	304,521	6,609	311,130	73,289	11,495	—	1,266,049
Other identifiable assets	—	—	—	—	—	—	106,430
Intercompany eliminations	—	(7,946)	(7,946)	—	—	—	—
Total	$2,934,799	$ —	$2,934,799	$695,692	$317,417	$366,037	$8,316,663
1994							
Electric	$2,126,581	$ 840	$2,127,421	$539,739	$252,273	$412,885	$5,981,634
Gas	421,249	—	421,249	27,801	32,478	76,091	726,759
Diversified businesses	235,155	8,245	243,400	67,719	11,199	—	1,200,551
Other identifiable assets	—	—	—	—	—	—	128,558
Intercompany eliminations	—	(9,085)	(9,085)	—	—	—	—
Total	$2,782,985	$ —	$2,782,985	$635,259	$295,950	$488,976	$8,037,502

Note 3. Subsidiary Information

Diversified businesses consist of the operations of the Constellation Companies, HP&S, EP&S, and Constellation Energy Source, Inc. (formerly named BNG, Inc.).

The Constellation Companies include Constellation Holdings, Inc., a wholly owned subsidiary which holds all of the stock of three other subsidiaries, Constellation Power, Inc. (formerly named Constellation Energy, Inc.), Constellation Investments, Inc., and Constellation Real Estate Group, Inc. These companies are engaged in development, ownership, and operation of power generation projects; financial investments; and development, ownership, and management of real estate and senior-living facilities, respectively.

HP&S is a wholly owned subsidiary which engages predominantly in the sales and service of electric and gas appliances, home improvements, and sales and service of heating and air conditioning systems, primarily in Central Maryland.

EP&S is a wholly owned subsidiary which provides a broad range of customized energy services. These energy services include: power quality services, customer electrical system improvements, lighting and mechanical engineering and installation services, campus and multi-building energy systems, energy consulting and financial contracts, district energy systems through Comfort Link (a partnership with the Poole and Kent Company), and, beginning in late 1996, private electric and gas distribution systems.

Constellation Energy Source, Inc. (formerly named BNG, Inc.) is a wholly owned subsidiary which engages in natural gas brokering.

BGE's investment in Safe Harbor Water Power Corporation, a producer of hydroelectric power, represents two-thirds of Safe Harbor's total capital stock, including one-half of the voting stock, and a two-thirds interest in its retained earnings.

The following is condensed financial information for the Constellation Companies. The condensed financial information does not reflect the elimination of intercompany balances or transactions which are eliminated in the Company's consolidated financial statements.

The 1996 operating results reflect a $14.6 million after-tax gain on the sale by a Constellation partnership of a power purchase agreement with Jersey Central Power & Light Company back to that utility. This gain was offset by a $7.0 million after-tax write-off of the investment in two geothermal wholesale power generating projects, a $3.0 million after-tax write-off of development costs of a proposed coal-fired power project that will not be built, and a $6.2 million after-tax write-off of a portion of an investment in a solar power project in which the Constellation Companies have a minority ownership interest and which is expected to be restructured with the lender.

	1996	1995	1994
		(In thousands, except per share amounts)	
Income Statements			
Revenues			
Real estate projects	$ 80,793	$ 108,414	$ 106,915
Power generation systems	93,134	57,734	41,301
Financial investments	38,916	25,201	12,126
Total revenues	212,843	191,349	160,342
Expenses other than interest and income taxes	113,247	114,479	107,267
Income from operations	99,596	76,870	53,075
Minority interest	(355)	(2,348)	—
Interest expense	(44,991)	(46,673)	(45,782)
Capitalized interest	14,645	13,582	10,776
Income tax benefit (expense)	(26,578)	(14,355)	(4,305)
Net income	$ 42,317	$ 27,076	$ 13,764
Contribution to the Company's earnings per share of common stock	$ .29	$ .18	$ .09
Balance Sheets			
Current assets	$ 115,689	$ 98,526	$ 92,814
Noncurrent assets	1,189,726	1,102,528	1,055,056
Total assets	$1,305,415	$1,201,054	$1,147,870
Current liabilities	$ 134,025	$ 70,393	$ 70,670
Noncurrent liabilities	775,237	778,505	758,626
Shareholder's equity	396,153	352,156	318,574
Total liabilities and shareholder's equity	$1,305,415	$1,201,054	$1,147,870

Note 4. Real Estate Projects and Financial Investments

Real Estate Projects

Real estate projects consist of the following investments held by the Constellation Companies:

At December 31,	1996	1995
	(In thousands)	
Properties under development	$286,200	$270,678
Rental and operating properties (net of accumulated depreciation)	237,725	207,666
Other real estate ventures	1,840	1,000
Total real estate projects	$525,765	$479,344

Financial Investments

Financial investments consist of the following investments held by the Constellation Companies:

At December 31,	1996	1995
	(In thousands)	
Insurance companies	$ 76,822	$ 77,792
Marketable equity securities	46,231	41,475
Financial limited partnerships	48,115	51,023
Leveraged leases	33,275	35,551
Total financial investments	$204,443	$205,841

Available-For-Sale Investments

The Constellation Companies' marketable equity securities shown above and BGE's investments comprising the nuclear decommissioning trust fund are classified as available-for-sale. The fair values, gross unrealized gains and losses, and amortized cost bases for available-for-sale securities, exclusive of $1.9 million of unrealized net gains on securities of equity-method investees, are as follows:

At December 31, 1996	Amortized Cost Basis	Unrealized Gains	Unrealized Losses	Fair Value
		(In thousands)		
Marketable equity securities	$ 39,363	$6,918	$ (50)	$ 46,231
U.S. government agency	18,167	263	—	18,430
State municipal bonds	73,571	2,202	(125)	75,648
Total	$131,101	$9,383	$(175)	$140,309

At December 31, 1995	Amortized Cost Basis	Unrealized Gains	Unrealized Losses	Fair Value
		(In thousands)		
Marketable equity securities	$ 38,520	$2,998	$ (43)	$ 41,475
U.S. government agency	14,177	141	—	14,318
State municipal bonds	50,411	2,056	(74)	52,393
Total	$103,108	$5,195	$(117)	$108,186

Gross and net realized gains and losses on the Constellation Companies' available-for-sale securities were as follows:

	1996	1995	1994
		(In thousands)	
Gross realized gains	**$4,280**	$5,470	$ 1,108
Gross realized losses	**(210)**	(2,446)	(3,150)
Net realized gains (losses)	**$4,070**	$3,024	$(2,042)

Contractual Maturities

The contractual maturities of debt securities are as follows:

	Amount
	(In thousands)
Less than 1 year	$ 1,000
1-5 years	10,065
5-10 years	71,405
More than 10 years	6,000
Total contractual maturities of debt securities	$88,470

Note 5. Regulatory Assets (net)

As discussed in Note 1, BGE's utility operations are subject to regulation by the Maryland Commission. Except for differences in the timing of the recognition of certain utility expenses and credits, the ratemaking process utilized by the Maryland Commission generally is based upon the same accounting principles applied by nonregulated entities. Under the Maryland Commission's ratemaking process, these utility expenses and credits are deferred on the Consolidated Balance Sheets as regulatory assets and liabilities and are recognized in income as the related amounts are included in service rates and recovered from or refunded to customers in utility revenues. The following table sets forth BGE's regulatory assets and liabilities:

At December 31,	1996	1995
	(In thousands)	
Income taxes recoverable through future rates	**$264,525**	$269,442
Deferred postemployment benefit costs	**89,217**	81,616
Deferred nuclear expenditures	**82,101**	86,519
Deferred environmental costs	**47,657**	38,371
Deferred energy conservation expenditures	**46,696**	73,297
Deferred cost of decommissioning federal uranium enrichment facilities	**46,015**	51,104
Deferred termination benefit costs	**41,137**	60,073
Deferred fuel costs	**22,734**	113,026
Deferred investment tax credits	**(133,970)**	(141,463)
Other	**6,167**	5,930
Total regulatory assets (net)	**$512,279**	$637,915

Income taxes recoverable through future rates represent principally the tax effect of depreciation differences not normalized and the allowance for equity funds used during construction, offset by unamortized deferred tax rate differentials and deferred taxes on deferred ITC. These amounts are amortized as the related temporary differences reverse. See Note 1 for a further discussion of income taxes.

Deferred postemployment benefit costs represent the excess of such costs recognized in accordance with Statements of Financial Accounting Standards No. 106 and No. 112 over the amounts reflected in utility rates. These costs will be amortized over a 15-year period beginning in 1998 (see Note 6).

Deferred nuclear expenditures represent the net unamortized balance of certain operations and maintenance costs which are being amortized over the remaining life of the Calvert Cliffs Nuclear Power Plant in accordance with orders of the Maryland Commission. These expenditures consist of costs incurred from 1979 through 1982 for inspecting and repairing seismic pipe supports, expenditures incurred from 1989 through 1994 associated with nonrecurring phases of certain nuclear operations projects, and expenditures incurred during 1990 for investigating leaks in the pressurizer heater sleeves.

Deferred environmental costs represent the estimated costs of investigating contamination and performing certain remediation activities at contaminated Company-owned sites (see Note 12). In November 1995, the Maryland Commission issued a rate order in the Company's gas base rate proceeding which authorized the Company to amortize over a 10-year period $21.6 million of these costs, the amount which had been incurred through October 1995.

Deferred energy conservation expenditures represent the net unamortized balance of certain operations costs which are being amortized over five years in accordance with orders of the Maryland Commission. These expenditures consist of labor, materials, and indirect costs associated with the conservation programs approved by the Maryland Commission.

Deferred cost of decommissioning federal uranium enrichment facilities represents the unamortized portion of BGE's required contributions to a fund for decommissioning and decontaminating the Department of Energy's (DOE) uranium enrichment facilities. The Energy Policy Act of 1992 requires domestic utilities to make such contributions, which are generally payable over a 15-year period with escalation for inflation and are based upon the amount of uranium enriched by DOE for each utility. These costs are being amortized over the contribution period as a cost of fuel.

Deferred termination benefit costs represent the net unamortized balance of the cost of certain termination benefits (see Note 7) applicable to BGE's regulated operations. These costs are being amortized over a five-year period in accordance with rate actions of the Maryland Commission.

Deferred fuel costs represent the difference between actual fuel costs and the fuel rate revenues under BGE's fuel clauses (see Note 1). Deferred fuel costs are reduced as they are collected from customers.

The underrecovered costs deferred under the fuel clauses were as follows:

At December 31,	1996	1995
	(In thousands)	
Electric deferred fuel costs		
Costs deferred	**$113,172**	$130,399
Reserve for disallowed replacement energy costs (see Note 12)	**(118,000)**	(35,000)
Net electric deferred fuel costs	**(4,828)**	95,399
Gas deferred fuel costs	**27,562**	17,627
Total deferred fuel costs	**$ 22,734**	$113,026

Deferred investment tax credits (ITC) represents ITC associated with BGE's regulated utility operations as discussed in Note 1. Deferred ITC are not deducted from rate base in accordance with federal income tax normalization requirements.

The foregoing regulatory assets and liabilities are recorded on BGE's Consolidated Balance Sheets in accordance with Statement of Financial Accounting Standards (SFAS) No. 71. If BGE were required to terminate application of SFAS No. 71 for all of its regulated operations, all such amounts deferred would be recognized in the Consolidated Statements of Income at that time, resulting in a charge to earnings, net of applicable income taxes.

Note 6. Pension and Postemployment Benefits

Pension Benefits

The Company sponsors several noncontributory defined benefit pension plans, the largest of which (the Pension Plan) covers substantially all BGE employees and certain employees of BGE's subsidiaries. The other plans, which are not material in amount, provide supplemental benefits to certain non-employee directors and key employees. Benefits under the plans are generally based on age, years of service, and compensation levels.

Prior service cost associated with retroactive plan amendments is amortized on a straight-line basis over the average remaining service period of active employees. The Company's funding policy is to contribute at least the minimum amount required under Internal Revenue Service regulations using the projected unit credit cost method. Plan assets at December 31, 1996 consisted primarily of marketable equity and fixed income securities, and group annuity contracts.

The following tables set forth the combined funded status of the plans and the composition of total net pension cost. Net pension cost shown below does not include the cost of termination benefits described in Note 7.

At December 31,	1996	1995
	(In thousands)	
Vested benefit obligation	$695,634	$688,084
Nonvested benefit obligation	17,974	15,668
Accumulated benefit obligation	713,608	703,752
Projected benefits related to increase in future compensation levels	132,673	122,539
Projected benefit obligation	846,281	826,291
Plan assets at fair value	(792,541)	(744,645)
Projected benefit obligation less plan assets	53,740	81,646
Unrecognized prior service cost	(21,890)	(24,357)
Unrecognized net loss	(117,157)	(118,361)
Unamortized net asset from adoption of FASB Statement No. 87	797	995
Accrued pension (asset) liability	$ (84,510)	$ (60,077)

Year Ended December 31,	1996	1995	1994
		(In thousands)	
Components of net pension cost			
Service cost-benefits earned during the period	$16,089	$11,407	$15,015
Interest cost on projected benefit obligation	59,948	58,433	58,723
Actual return on plan assets	(57,671)	(150,510)	7,932
Net amortization and deferral	2,115	94,674	(60,071)
Total net pension cost	20,481	14,004	21,599
Amount capitalized as construction cost	(2,442)	(1,422)	(2,578)
Amount charged to expense	$18,039	$12,582	$19,021

The Company also sponsors a defined contribution savings plan covering all eligible BGE employees and certain employees of BGE's subsidiaries. Under this plan, the Company makes contributions on behalf of participants. Company contributions to this plan totaled $9.4 million, $8.5 million, and $8.7 million in 1996, 1995, and 1994, respectively.

Postretirement Benefits

The Company sponsors defined benefit postretirement health care and life insurance plans which cover substantially all BGE employees and certain employees of its subsidiaries. Benefits under the plans are generally based on age, years of service, and pension benefit levels. The postretirement benefit (PRB) plans are unfunded. Substantially all of the health care plans are contributory, and participant contributions for employees who retire after June 30, 1992 are based on age and years of service. Retiree contributions increase commensurate with the expected increase in medical costs. The postretirement life insurance plan is noncontributory. The transition obligation resulting from the adoption of Statement of Financial Accounting Standards No. 106 effective January 1, 1993 is being amortized over a 20-year period.

In April 1993, the Maryland Commission issued a rate order authorizing BGE to recognize in operating expense one-half of the annual increase in PRB costs applicable to regulated operations as a result of the adoption of Statement No. 106 and to defer the remainder of the annual increase in these costs for inclusion in BGE's next base rate proceeding. In accordance with the April 1993 Order, all amounts to be deferred prior to completion of BGE's next base rate proceeding will be amortized over a 15-year period beginning in 1998.

In November 1995, the Maryland Commission issued a rate order in BGE's gas base rate proceeding providing for full recognition in operating expense of PRB and other postemployment benefits (discussed below) costs attributable to gas operations, and affirming its previous decision on amortization of deferred PRB costs. This phase-in approach meets the guidelines established by the Emerging Issues Task Force of the Financial Accounting Standards Board for deferring PRB costs as a regulatory asset. Accrual-basis PRB costs applicable to nonregulated operations are charged to expense.

The following table sets forth the components of the accumulated PRB obligation and a reconciliation of these amounts to the accrued PRB liability.

At December 31,	1996		1995	
	Health Care	Life Insurance	Health Care	Life Insurance
	(In thousands)			
Accumulated postretirement benefit obligation:				
Retirees	$163,904	$45,485	$157,804	$44,769
Active employees	82,373	19,269	84,724	18,599
Total accumulated postretirement benefit obligation	246,277	64,754	242,528	63,368
Unrecognized transition obligation	(141,089)	(40,960)	(149,907)	(43,521)
Unrecognized net loss	(7,368)	(5,690)	(12,767)	(5,764)
Accrued postretirement benefit liability	$ 97,820	$18,104	$ 79,854	$14,083

The following table sets forth the composition of net PRB cost. Such cost does not include the cost of termination benefits described in Note 7.

Year ended December 31,	1996	1995
	(In thousands)	
Net postretirement benefit cost:		
Service cost—benefits earned during the period	$ 5,559	$ 3,918
Interest cost on accumulated post retirement benefit obligation	21,918	21,203
Amortization of transition obligation	11,378	11,378
Net amortization and deferral	174	(86)
Total net postretirement benefit cost	39,029	36,413
Amount capitalized as construction cost	(6,224)	(5,299)
Amount deferred	(7,455)	(8,025)
Amount charged to expense	$25,350	$23,089

Other Postemployment Benefits

The Company provides health and life insurance benefits to employees of BGE and certain employees of its subsidiaries who are determined to be disabled under BGE's Disability Insurance Plan. The Company also provides pay continuation payments for employees determined to be disabled before November 1995. Such payments for employees determined to be disabled after that date are paid by an insurance company, and the cost of such insurance is paid by employees. The liability for these benefits totaled $51 million and $52 million as of December 31, 1996 and 1995, respectively. The portion of the liability attributable to regulated activities as of December 31, 1993 was deferred.

Consistent with the Maryland Commission's November 1995 order, the amounts deferred will be amortized over a 15-year period beginning in 1998.

Assumptions

The pension, postretirement, and other postemployment benefit liabilities were determined using the following assumptions.

At December 31,	1996	1995
Assumptions:		
Discount rate		
Pension and postretirement benefits	7.5%	7.5%
Other postemployment benefits	6.0	6.0
Average increase in future compensation levels	4.0	4.0
Expected long-term rate of return on assets	9.0	9.0

The health care inflation rates for 1996 are assumed to be 9.5% for Medicare-eligible retirees and 8.9% for retirees not covered by Medicare. The health care inflation rates for 1997 are assumed to be 7.5% for Medicare-eligible retirees and 10.0% for retirees not covered by Medicare. After 1997 both rates are assumed to decrease by 0.5% annually to an ultimate rate of 5.5% in the years 2001 and 2006, respectively. A one percentage point increase in the health care inflation rate from the assumed rates would increase the accumulated postretirement benefit obligation by approximately $41 million as of December 31, 1996 and would increase the aggregate of the service cost and interest cost components of postretirement benefit cost by approximately $4 million annually.

Note 7. Termination Benefits

BGE offered a Voluntary Special Early Retirement Program (the 1992 VSERP) to eligible employees who retired during the period February 1, 1992 through April 1, 1992. In April 1993, the Maryland Commission authorized BGE to amortize the $6.6 million cost of termination benefits associated with the 1992 VSERP, which consisted principally of an enhanced pension benefit, over a five-year period for ratemaking purposes.

BGE offered a second Voluntary Special Early Retirement Program (the 1993 VSERP) to eligible employees who retired as of February 1, 1994. The one-time cost of the 1993 VSERP consisted of enhanced pension and postretirement benefits. In addition to the 1993 VSERP, further employee reductions have been accomplished through the elimination of certain positions, and various programs have been offered to employees impacted by the eliminations. The $88.3 million portion of 1993 VSERP attributable to regulated activities was deferred and is being amortized over a five-year period for ratemaking purposes, beginning in February 1994, consistent with previous rate actions of the Maryland Commission.

Note 8. Short-Term Borrowings

Short-term borrowings include bank loans, commercial paper notes, and bank lines of credit. The Company pays commitment fees in support of lines of credit. Borrowings under the lines are at the banks' prime rates, base interest rates, or at various money market rates.

Short-term borrowings were as follows:

At December 31,	**1996**	1995
	(In thousands)	
BGE's bank loans	**$ 8,785**	$ 3,845
BGE's commercial paper notes	**324,400**	275,300
Constellation Companies' lines of credit	—	160
Total short-term borrowings	**$333,185**	$279,305

The weighted average interest rates for short-term borrowings were as follows:

Year ended December 31,	**1996**	1995
BGE		
Bank loans	**4.93%**	4.74%
Commercial Paper Notes	**5.53**	5.92
Constellation Companies		
Lines of Credit	**—**	—

Unused lines of credit supporting commercial paper notes at December 31, 1996 and 1995 were $203 million and $238 million, respectively. These amounts are exclusive of $150 million of revolving credit agreements undrawn at year-end (see Note 9).

Note 9. Long-Term Debt

First Refunding Mortgage Bonds of BGE

Substantially all of the principal properties and franchises owned by BGE, as well as the capital stock of Constellation Holdings, Inc., Safe Harbor Water Power Corporation, HP&S, EP&S, and Constellation Energy Source, Inc. (formerly named BNG, Inc.), are subject to the lien of the mortgage under which BGE's outstanding First Refunding Mortgage Bonds have been issued.

On August 1 of each year, BGE is required to pay to the mortgage trustee an annual sinking fund payment equal to 1% of the largest principal amount of Mortgage Bonds outstanding under the mortgage during the preceding twelve months. Such funds are to be used, as provided in the mortgage, for the purchase and retirement by the trustee of Mortgage Bonds of any series other than the 5½% Installment Series of 2002, the 8.40% Series of 1999, the 5½% Series of 2000, the 8⅛% Series of 2001, the 7⅛% Series of 2002, the 6½% Series of 2003, the 6⅛% Series of 2003, the 5½% Series of 2004, the 7½% Series of 2007, and the 6⅛% Series of 2008.

The principal amounts of the 5½% Installment Series Mortgage Bonds payable each year are as follows:

Year	
	(In thousands)
1997	$ 605
1998 and 1999	690
2000 and 2001	865
2002	6,725

The Remarketed Floating Rate Series Due September 1, 2006 First Refunding Mortgage Bonds include a provision that allows the bondholders the option to tender their bonds back to BGE on an annual basis. BGE is required to repurchase and retire at par any bonds tendered that are not remarketed or purchased by the remarketing agent. In addition, BGE has the option to call the bonds annually at par on each remarketing date.

Other Long-Term Debt of BGE

BGE maintains revolving credit agreements that expire at various times from 1997 through 1999. Under the terms of the agreements, BGE may, at its option, obtain loans at various interest rates. A commitment fee is paid on the daily average of the unborrowed portion of the commitment. At December 31, 1996, BGE had no borrowings under these revolving credit agreements and had available $150 million of unused capacity under these agreements.

Under the terms of the bank loan which matures on March 29, 2001, the bank has a one-time option to cancel the loan on December 29, 1997. Until that date, the interest rate on the loan is 5.22%. If the bank does not cancel the loan on December 29, 1997, the interest rate for the remaining term will reset to 6.11%.

Following is information regarding BGE's Medium-term Notes outstanding at December 31, 1996:

Series	Weighted-Average Interest Rate	Maturity Dates
B	8.43%	1998-2006
C	7.09%	1997-2003
D	6.60%	1998-2006

Long-Term Debt of Constellation Companies

The Constellation Companies have a $75 million unsecured revolving credit agreement which matures December 9, 1999 and is used to provide liquidity for general corporate purposes. A commitment fee is paid on the daily average of the unborrowed portion of the commitment. At December 31, 1996, the Constellation Companies had $65 million outstanding under this agreement.

The Constellation Companies' mortgage and construction loans and other collateralized notes have varying terms. The 8.00% mortgage note requires monthly principal and interest payments through July 31, 2001. The 8.00% construction loan requires no monthly principal and interest payments during construction and is due October 30, 2003. The variable rate mortgage notes require periodic payment of principal and interest with various maturities from June 1997 through July 2009. The 7.50% mortgage note requires monthly principal and interest payments through October 9, 2005. The 7.357% mortgage note requires quarterly principal and interest payments through March 15, 2009. The 9.65% mortgage note requires monthly principal and interest payments through February 1, 2028.

The unsecured notes outstanding as of December 31, 1996 mature in accordance with the following schedule:

	Amount
	(In thousands)
8.93%, due August 28, 1997	$ 52,000
6.65%, due September 9, 1997	15,000
8.23%, due October 15, 1997	30,000
7.05%, due April 22, 1998	25,000
7.06%, due September 9, 1998	20,000
8.48%, due October 15, 1998	75,000
7.30%, due April 22, 1999	90,000
8.73%, due October 15, 1999	15,000
7.55%, due April 22, 2000	35,000
7.43%, due September 9, 2000	30,000
8.00%, due December 31, 2000	160
Total unsecured notes	$387,160

Long-Term Debt of Other Diversified Businesses

Long-term debt of other diversified businesses includes a $50 million unsecured revolving credit agreement of Comfort Link which matures September 26, 2001. Loans may be obtained at various rates for terms up to nine months. A facility fee is paid on the total amount of the commitment. At December 31, 1996, $12 million was outstanding under this agreement.

Weighted Average Interest Rates for Variable Rate Debt

The weighted average interest rates for variable rate debt were as follows:

Year ended December 31,	1996	1995
BGE		
Floating rate series mortgage bonds	5.87%	6.30%
Remarketed floating rate series mortgage bonds	5.63	—
Pollution control loan	3.49	3.79
Port facilities loan	3.59	4.06
Adjustable rate pollution control loan	3.90	3.75
Economic development loan	3.57	4.01
Constellation Companies		
Loans under credit agreements	6.08	6.74
Mortgage and construction loans and other collateralized notes	8.33	8.99
Other Diversified Businesses		
Loans under credit agreements	6.13	—

Aggregate Maturities

The combined aggregate maturities and sinking fund requirements for all of the Company's long-term borrowings for each of the next five years are as follows:

Year	BGE	Diversified Businesses
	(In thousands)	
1997	$ 89,848	$107,924
1998	93,578	165,370
1999	247,347	186,339
2000	253,658	97,803
2001	247,183	31,897

As of December 31, 1996, BGE had $195 million of debt with provisions that allow lenders the option to request BGE to repay the debt at certain times prior to maturity. In the event such options are exercised, BGE intends to refinance such debt on a long-term basis through the issuance of medium term notes or using revolving credit agreements.

Note 10. Redeemable Preference Stock

The 7.80%, 1989 Series is subject to mandatory redemption in full at par on July 1, 1997. The following series are subject to an annual mandatory redemption of the number of shares shown below at par beginning in the year shown below. At BGE's option, an additional number of shares, not to exceed the same number as are mandatory, may be redeemed at par in any year, commencing in the same year in which the mandatory redemption begins. The 8.25%, 1989 Series, the 8.625%, 1990 Series, and the 7.85%, 1991 Series listed below are not redeemable except through operation of a sinking fund.

Series	Shares	Beginning Year
7.50%, 1986 Series	15,000	1992
6.75%, 1987 Series	15,000	1993
8.25%, 1989 Series	100,000	1995
8.625%, 1990 Series	130,000	1996
7.85%, 1991 Series	70,000	1997

The combined aggregate redemption requirements at December 31, 1996 for all series of redeemable preference stock are as follows:

Year	
	(In thousands)
1997	$ 83,000
1998	23,000
1999	23,000
2000	10,000
2001	10,000
Thereafter	68,500
Total aggregate redemption requirements	$217,500

With regard to payment of dividends or assets available in the event of liquidation, all issues of preference stock, whether subject to mandatory redemption or not, rank equally; and all preference stock ranks prior to common stock.

Note 11. Leases

The Company, as lessee, contracts for certain facilities and equipment under lease agreements with various expiration dates and renewal options. Consistent with the regulatory treatment, lease payments for utility operations are charged to expense. Lease expense, which is comprised primarily of operating leases, totaled $11.6 million, $12.2 million, and $12.7 million for the years ended 1996, 1995, and 1994, respectively.

The future minimum lease payments at December 31, 1996 for long-term noncancelable operating leases are as follows:

Year	*(In thousands)*
1997	$ 4,899
1998	4,095
1999	2,072
2000	1,893
2001	1,450
Thereafter	2,725
Total minimum lease payments	$17,134

Certain of the Constellation Companies, as lessor, have entered into operating leases for office and retail space. These leases expire over periods ranging from 1 to 19 years, with options to renew. The net book value of property under operating leases was $177.3 million at December 31, 1996. The future minimum rentals to be received under operating leases in effect at December 31, 1996 are as follows:

Year	*(In thousands)*
1997	$ 15,433
1998	14,073
1999	13,146
2000	12,671
2001	11,704
Thereafter	61,735
Total minimum rentals	$128,762

Note 12. Commitments, Guarantees, and Contingencies

Commitments

BGE has made substantial commitments in connection with its construction program for 1997 and subsequent years. In addition, BGE has entered into three long-term contracts for the purchase of electric generating capacity and energy. The contracts expire in 2001, 2013, and 2023. Total payments under these contracts were $64.1, $68.4, and $69.4 million during 1996, 1995, and 1994, respectively. At December 31, 1996, the estimated future payments for capacity and energy that BGE is obligated to buy under these contracts are as follows:

Year	*(In thousands)*
1997	$ 61,669
1998	78,075
1999	91,938
2000	92,039
2001	62,978
Thereafter	805,110
Total estimated future payments for capacity and energy under long-term contracts	$1,191,809

Certain of the Constellation Companies have committed to contribute additional capital and to make additional loans to certain affiliates, joint ventures, and partnerships in which they have an interest. As of December 31, 1996, the total amount of investment requirements committed to by the Constellation Companies is $56 million.

In December, 1994, BGE and HP&S entered into agreements with a financial institution whereby BGE and HP&S can sell on an ongoing basis up to an aggregate of $40 million and $50 million, respectively, of an undivided interest in a designated pool of customer receivables. Under the terms of the agreements, BGE and HP&S have limited recourse on the receivables and have recorded a reserve for credit losses. At December 31, 1996, BGE and HP&S had sold $35 million and $47 million of receivables, respectively, under these agreements.

Guarantees

BGE has agreed to guarantee two-thirds of certain indebtedness of Safe Harbor Water Power Corporation. The total amount of indebtedness that can be guaranteed is $50 million, of which $33 million represents BGE's potential share of the guarantee. As of December 31, 1996, outstanding indebtedness of Safe Harbor Water Power Corporation was $32 million, of which $21 million is guaranteed by BGE. BGE has also agreed to guarantee up to $20 million of obligations and indebtedness of Constellation Energy Source, Inc. (formerly named BNG, Inc.) As of December 31, 1996, there were no outstanding obligations under this guarantee. BGE assesses that the risk of material loss on the loans guaranteed is minimal.

As of December 31, 1996, the total outstanding loans and letters of credit of certain power generation and real estate projects guaranteed by the Constellation Companies were $54 million. Also, the Constellation Companies have agreed to guarantee certain other borrowings of various power generation and real estate projects. The Company has assessed that the risk of material loss on the loans guaranteed and performance guarantees is minimal.

Pending Merger With Potomac Electric Power Company

BGE, Potomac Electric Power Company (PEPCO), and Constellation Energy Corporation (formerly named "RH Acquisition Corp.") (CEC), have entered into an Agreement and Plan of Merger, dated as of September 22, 1995 (the Merger Agreement). CEC was formed to accomplish the merger and its outstanding capital stock is owned 50% by BGE and 50% by PEPCO. The Merger Agreement provides for a strategic business combination that will be accomplished by merging both BGE and PEPCO into CEC (the Merger). The Merger, which was unanimously approved by the Boards of Directors of BGE and PEPCO and approved by the shareholders of both companies, is expected to close during 1997 after all other conditions to the consummation of the Merger, including obtaining applicable regulatory approvals (described below), are met or waived. In connection with the Merger, BGE common shareholders will receive one share of CEC common stock for each BGE share and PEPCO common shareholders will receive 0.997 of a share of CEC common stock for each PEPCO share.

Preliminary estimates by the managements of PEPCO and BGE indicate that the synergies resulting from the combination of their utility operations could generate net cost savings of up to $1.3 billion over a period of 10 years following the Merger. These estimates indicate that about two-thirds of the savings will come from reduced labor costs, with the remaining savings split between nonfuel purchasing and corporate and administrative programs. These savings are net of costs to achieve, presently estimated to be approximately $150 million, and are expected to be allocated among shareholders and customers. This allocation will depend upon the results of regulatory proceedings in the various jurisdictions in which BGE and PEPCO operate their utility businesses (see discussion of the issues raised in regulatory proceedings regarding the allocation and other matters). The analyses employed in order to develop estimates of the potential savings as a result of the Merger were necessarily based upon various assumptions which involve judgments with respect to, among other things, future national and regional economic and competitive conditions, inflation rates, regulatory treatment, weather conditions, financial market conditions, interest rates, future business decisions and other uncertainties, all of which are difficult to predict and many of which are beyond the control of BGE and PEPCO. Accordingly, while BGE believes that such assumptions are reasonable for purposes of the development of estimates of potential savings, there can be no assurance that such assumption will approximate actual experience or that all such savings will be realized.

Major regulatory proceedings, together with an indication of the current status of the proceeding, which must be concluded in order to proceed with the merger, are listed below. The Merger Agreement provides that a condition to closing is that no such approvals shall impose terms and conditions that would have, or would be reasonably likely to have, a material adverse effect on the business, operations, properties, assets, condition (financial or otherwise), prospects, or results of operations of the new company.

■ *Federal Energy Regulatory Commission (FERC)* - Hearings have been completed and we are waiting for a decision. The hearings explored the merged company's generation market power, including the appropriate geographic markets, and to consider appropriate remedies if the merged company is found to possess generation market power. Testimony of FERC staff included the suggestion that a significant portion of generation (approximately 2400-3600 megawatts) be divested or transmission capability be upgraded or both due to the perceived market power of the merged company in both the wholesale and retail markets.

■ *Maryland Public Service Commission (Maryland Commission)* - Hearings have been completed and we are waiting for a decision. Since the Report on Form 10-Q for the third quarter 1996 was filed, rebuttal and surrebuttal testimony has been filed. Office of People's Counsel (the advocates for residential customers) recommended that the Maryland Commission not approve the Merger until the Applicants demonstrate that Maryland customers will not be harmed by potential restrictions on competition due to the market power of the new company. If, however, the Maryland Commission decides to approve the Merger, People's Counsel continues to recommend rate decreases. Due to the use of a different test period, the amounts are somewhat different than reported in the second quarter Report on Form 10-Q. Based on a test period proposed by People's Counsel in recent testimony, they recommend a pre-merger rate reduction of approximately $108.3 million ($84.7 million to BGE customers and $23.6 million to PEPCO customers) with Merger savings being reflected in further reduced rates of approximately $65 million ($45 million to BGE customers and $20 million to PEPCO customers) contemporaneously with the date of the Merger. A number of other recommendations are also included in People's Counsel testimony. The Maryland Energy Administration (MEA) continues to recommend that the Maryland Commission adopt an alternative regulatory plan and also asks that rates be examined. Maryland Commission Staff testimony also utilizes the new test period. Based on the new test period Maryland Commission Staff recommends an immediate decrease of $63.6 million (BGE's rates reduced by $54.3 million and PEPCO by $9.3 million) at the time of the Merger. Maryland Commission Staff's surrebuttal testimony also recommends that CEC be required to make a rate filing 15 months after the Merger becomes effective.

■ *District of Columbia Public Service Commission* - Hearings began February 18, 1997. Testimony was filed by the parties in September 1996. The D.C. Office of People's Counsel (the advocates for residential customers) opposes the Merger based on its contention that BGE and PEPCO have not proved that the Merger is in the public interest. Testimony of the D.C. People's Counsel also provides that should the Merger be approved, an immediate rate reduction of $44.2 million be imposed at the time of the Merger, followed by a 5-year moratorium on rate increases. Further, testimony of D.C. People's Counsel advocates divestiture of all nonutility affiliate companies, exclusion of BGE's Calvert Cliffs Nuclear Plant from production plant assigned to D.C., and a 5-year $23.37 million per year economic development program. GSA, a major D.C. customer, requests that any approval should be coupled with an imposition of retail competition access for ratepayers such as GSA, a 25-year amortization of costs to achieve the Merger, and elimination of Calvert Cliffs from the generating mix. In addition to these matters, D.C. People's Counsel, an intervenor, Washington Gas Light Company, and the D.C. Corporation Counsel have questioned the interpretation by BGE and PEPCO that a D.C. statute known as the Antimerger Law is inapplicable to this transaction. Should such statute be deemed to be applicable, authorization of the Merger by Congress would be required. Allegations also were made that BGE and PEPCO should have received Congressional approval for their owning 50% of the shell company, CEC, prior to consummation of the Merger.

The reasons for the Merger, the terms and conditions contained in the Merger Agreement, the regulatory approvals required prior to closing the Merger, and other matters concerning the Merger, PEPCO, and CEC are discussed in more detail in the Registration Statement on Form S-4 (Registration No. 33-64799).

Environmental Matters

The Clean Air Act of 1990 (the Act) contains two titles designed to reduce emissions of sulfur dioxide and nitrogen oxide (NOx) from electric generating stations. Title IV contains provisions for compliance in two separate phases. Phase I of Title IV became effective January 1, 1995, and Phase II of Title IV must be implemented by 2000. BGE met the requirements of Phase I by installing flue gas desulfurization systems and fuel switching and through unit retirements. BGE is currently examining what actions will be required in order to comply with Phase II of the Act. However, BGE anticipates that compliance will be attained by some combination of fuel switching, flue gas desulfurization, unit retirements, or allowance trading.

At this time, plans for complying with NOx control requirements under Title I of the Act are less certain because all implementation regulations have not yet been finalized by the government. It is expected that by the year 1999 these regulations will require additional NOx controls for ozone attainment at BGE's generating plants and at other BGE facilities. The controls will result in additional expenditures that are difficult to predict prior to the issuance of such regulations. Based on existing and proposed ozone nonattainment regulations, BGE currently estimates that the NOx controls at BGE's generating plants will cost approximately $90 million. BGE is currently unable to predict the cost of compliance with the additional requirements at other BGE facilities.

BGE has been notified by the Environmental Protection Agency and several state agencies that it is being considered a potentially responsible party (PRP) with respect to the cleanup of certain environmentally contaminated sites owned and operated by third parties. Cleanup costs for these sites cannot be estimated, except that BGE's 15.79% share of the possible cleanup costs at one of these sites, Metal Bank of America, a metal reclaimer in Philadelphia, could exceed amounts recognized by up to approximately $7 million based on the highest estimate of costs in the range of reasonably possible alternatives. Although the cleanup costs for certain of the remaining sites could be significant, BGE believes that the resolution of these matters will not have a material effect on its financial position or results of operations.

Also, BGE is coordinating investigation of several former gas manufacturing plant sites, including exploration of corrective action options to remove coal tar. In late December 1996, the Maryland Department of the Environment and BGE signed a consent order that requires BGE to implement remedial action plans addressing contamination at and related to the Spring Gardens site. The specific remedial actions for this site will be developed in the future. BGE has recognized estimated environmental costs at all former gas manufacturing plant sites (based on remedial action options) which are considered probable totaling $50 million in nominal dollars. These costs, net of accumulated amortization, have been deferred as a regulatory asset (see Note 5). Accounting rules also require BGE to disclose additional costs deemed by BGE to be less likely than probable costs, but still "reasonably possible" of being incurred at these sites. Because of the results of recent studies at these sites, it is reasonably possible that these additional costs could exceed the amount recognized by approximately $48 million in nominal dollars ($11 million in current dollars, plus the impact of inflation at 3.1% over a period of up to 60 years).

Nuclear Insurance

An accident or an extended outage at either unit of the Calvert Cliffs Nuclear Power Plant could have a substantial adverse effect on BGE. The primary contingencies resulting from an incident at the Calvert Cliffs plant would involve the physical damage to the plant, the recoverability of replacement power costs, and BGE's liability to third parties for property damage and bodily injury. BGE maintains various insurance policies for these contingencies. The costs that could result from a major accident or an extended outage at either of the Calvert Cliffs units could exceed the coverage limits.

In addition, in the event of an incident at any commercial nuclear power plant in the country, BGE could be assessed for a portion of any third party claims associated with the incident. Under the provisions of the Price Anderson Act, the limit for third party claims from a nuclear incident is $8.92 billion. If third party claims relating to such an incident exceed $200 million (the amount of primary insurance), BGE's share of the total liability for third party claims could be up to $159 million per incident, that would be payable at a rate of $20 million per year.

BGE and other operators of commercial nuclear power plants in the United States are required to purchase insurance to cover claims of certain nuclear workers. Other non-governmental commercial nuclear facilities may also purchase such insurance. Coverage of up to $400 million is provided for claims against BGE or others insured by these policies for radiation injuries. If certain claims were made under these policies, BGE and all policyholders could be assessed, with BGE's share being up to $6.02 million in any one year.

For physical damage to Calvert Cliffs, BGE has $2.75 billion of property insurance from industry mutual insurance companies. If an outage at Calvert Cliffs is caused by an insured physical damage loss and lasts more than 21 weeks, BGE has up to $473.2 million per unit of insurance, provided by an industry mutual insurance company, for replacement power costs. This amount can be reduced by up to $94.6 million per unit if an outage to both units at Calvert Cliffs is caused by a singular insured physical damage loss. If accidents at any insured plants cause a shortfall of funds at the industry mutuals, BGE and all policyholders could be assessed, with BGE's share being up to $35.1 million.

Recoverability of Electric Fuel Costs

By statute, actual electric fuel costs are recoverable so long as the Maryland Commission finds that BGE demonstrates that, among other things, it has maintained the productive capacity of its generating plants at a reasonable level. The Maryland Commission and Maryland's highest appellate court have interpreted this as permitting a subjective evaluation of each unplanned outage at BGE's generating plants to determine whether or not BGE had implemented all reasonable and cost-effective maintenance and operating control procedures appropriate for preventing the outage. Effective January 1, 1987, the Maryland Commission authorized the establishment of a Generating Unit Performance Program (GUPP) to measure, annually, utility compliance with maintaining the productive capacity of generating plants at reasonable levels by establishing a system-wide generating performance target and individual performance targets for each base load generating unit. In fuel rate hearings, actual generating performance after adjustment for planned outages will be compared to the system-wide target and, if met, should signify that BGE has complied with the requirements of Maryland law. Failure to meet the system-wide target will result in review of each unit's adjusted actual generating performance versus its performance target in determining compliance with the law and the basis for possibly imposing a penalty on BGE. Parties to fuel rate hearings may still question the prudence of BGE's actions or inactions with respect to any given generating plant outage, which could result in the disallowance of replacement energy costs by the Maryland Commission.

Since the two units at BGE's Calvert Cliffs Nuclear Power Plant utilize BGE's lowest cost fuel, replacement energy costs associated with outages at these units can be significant. BGE cannot estimate the amount of replacement energy costs that could be challenged or disallowed in future fuel rate proceedings, but such amounts could be material.

In October 1988, BGE filed its first fuel rate application for a change in its electric fuel rate under GUPP. The resultant case before the Maryland Commission covers BGE's operating performance in calendar year 1987, and BGE's filing demonstrated that it met the system-wide and individual nuclear plant performance targets for 1987. In November 1989, testimony was filed on behalf of the Maryland People's Counsel (People's Counsel) alleging that seven outages at the Calvert Cliffs plant in 1987 were due to management imprudence and that the replacement energy costs associated with those outages should be disallowed by the Commission. Total replacement energy costs associated with the 1987 outages were approximately $33 million. On January 23, 1995, the Hearing Examiner issued his decision in the 1987 fuel rate proceeding and found that the Company had met the GUPP standard which establishes a presumption that BGE had operated the plant at a reasonably productive capacity level. However, the Order found that the presumption of reasonableness would be overcome by a showing of mismanagement and that such a showing was made with respect to the environmental qualifications outage time. The Hearing Examiner had mitigated the disallowance of replacement energy costs due to the fact the GUPP standard was met. The Hearing Examiner's Order was appealed to the Maryland Commission by both BGE and People's Counsel. The Maryland Commission upheld the Hearing Examiner's findings with respect to the environmental

qualification related outage time, but disagreed with certain methodologies applied by the Hearing Examiner. The impact of the Maryland Commission's decision on the Company's 1996 earnings was approximately $4.5 million, the amount previously estimated by the Company. People's Counsel has filed a motion for rehearing.

In May 1989, BGE filed its fuel rate case in which 1988 performance was examined. BGE met the system-wide and nuclear plant performance targets in 1988. People's Counsel alleged that BGE imprudently managed several outages at Calvert Cliffs, and BGE estimates that the total replacement energy costs associated with these 1988 outages were approximately $2 million. On November 14, 1991, a Hearing Examiner at the Maryland Commission issued a proposed Order, which became final on December 17, 1991 and concluded that no disallowance was warranted. The Hearing Examiner found that BGE maintained the productive capacity of the Plant at a reasonable level, noting that it produced a near record amount of power and exceeded the GUPP standard. Based on this record, the Order concluded there was sufficient cause to excuse any avoidable failures to maintain productive capacity at higher levels.

During 1989, 1990, and 1991, BGE experienced extended outages at its Calvert Cliffs Nuclear Power Plant. In the Spring of 1989, a leak was discovered around the Unit 2 pressurizer heater sleeves during a refueling outage. BGE shut down Unit 1 as a precautionary measure on May 6, 1989, to inspect for similar leaks and none were found. However, Unit 1 was out of service for the remainder of 1989 and 285 days of 1990 to undergo maintenance and modification work to enhance the reliability of various safety systems, to repair equipment, and to perform required periodic surveillance tests. Unit 2, which returned to service May 4, 1991, remained out of service for the remainder of 1989, 1990, and the first part of 1991 to repair the pressurizer, perform maintenance and modification work, and complete the refueling. The replacement energy costs associated with these extended outages for both units at Calvert Cliffs, concluding with the return to service of Unit 2, are estimated to be $458 million.

In a December 1990 Order issued by the Maryland Commission in a BGE base rate proceeding, the Maryland Commission found that certain operations and maintenance expenses incurred at Calvert Cliffs during the test year should not be recovered from ratepayers. The Maryland Commission found that this work, which was performed during the 1989-1990 Unit 1 outage and fell within the test year, was avoidable and caused by BGE actions which were deficient. The Maryland Commission noted in the Order that its review and findings on these issues pertain to the reasonableness of BGE's test year operations and maintenance expenses for purposes of setting base rates and not to the responsibility for replacement energy costs associated with the outages at Calvert Cliffs. The Maryland Commission stated that its decision in the base rate case will have no res judicata (binding) effect in the fuel rate proceeding examining the 1989-1991 outages. The work characterized as avoidable significantly increased the duration of the Unit 1 outage. Despite the Maryland Commission's statement regarding no binding effect, BGE recognizes that the views expressed by the Maryland Commission made the full recovery of all of the replacement energy costs associated with the Unit 1 outage doubtful. Therefore, in December 1990, BGE recorded a provision of $35 million against the possible disallowance of such costs.

In December 1996, BGE entered into a settlement agreement with People's Counsel and the Maryland Commission Staff proposing a resolution to these fuel rate proceedings. BGE agreed that ratepayers will not fund a total of $118 million of electric replacement energy costs associated with the extended outages. This represents $83 million in addition to the $35 million reserve for possible disallowance of replacement energy costs recorded in 1990. Therefore, in December 1996, BGE increased the provision for the disallowance of such costs by $83 million. Additionally, in 1996, BGE wrote off $5.6 million of accrued carrying charges related to the deferred fuel balances. The remainder of the replacement energy costs associated with the extended outage has already been recovered from customers through the fuel rate.

California Power Purchase Agreements

The Constellation Companies have ownership interests in 16 projects that sell electricity in California under "Interim Standard Offer No. 4" power purchase agreements. Under these agreements, the projects supply electricity to utilities at a fixed rate for capacity and energy the first 10 years of the agreements, and a fixed rate for capacity plus a variable rate for energy based on the utilities' avoided cost for the remaining term of the agreements. Avoided cost generally is the cost of a utility's lowest-cost next-available source of generation to service the demands on its system.

From 1996 through 2000, the 10-year periods for fixed energy rates expire for these projects and they will begin supplying electricity at variable rates. At current avoided cost levels, the Constellation Companies would experience reduced earnings or incur losses associated with these projects when they begin supplying electricity at variable rates. Eight projects begin supplying electricity at variable rates in 1997 and 1998. The projects that make the highest revenues will begin supplying electricity at variable rates in 1999 and 2000. As a result, we do not expect the Constellation Companies to experience significantly lower earnings or losses on these projects before 2000. Constellation is pursuing alternatives for these power generation projects including repowering the projects to reduce operating costs, changing fuels to reduce operating costs, renegotiating the power purchase agreements to improve the terms, restructuring financings to improve the financing terms, and selling its ownership interests in the projects. The Company cannot estimate the financial impact of the switch from fixed to variable rates on the Constellation Companies or on BGE, but the impact could be material.

Constellation Real Estate

Management will consider market demand, interest rates, the availability of financing, and the strength of the economy in general when making decisions about real estate investments. We believe until the economy shows sustained growth and there is more demand for new development, real estate values will not improve much. If we were to sell our real estate projects in the current market, we would have losses, although the amount of the losses is hard to predict. Management's current real estate strategy is to hold each real estate project until we can realize a reasonable value for it. Management evaluates strategies for all its businesses, including real estate, on an ongoing basis. Competing demands for our financial resources, changes in the utility industry, and the proposed merger with Potomac Electric Power Company, are factors we will consider when we evaluate all diversified business strategies so we use capital and other resources effectively. Depending on market conditions in the future, we could also have losses on any future sales.

Applicable accounting rules would require a writedown of a real estate investment to market value in either of two cases. The first is if we change our intent about a project from an intent to hold to an intent to sell and the market value of that project is below book value. The second is if the expected cash flow from the project is less than the investment in the project.

Note 13. Fair Value of Financial Instruments

The following table presents the carrying amounts and fair values of financial instruments included in the Consolidated Balance Sheets.

At December 31,	1996		1995	
	Carrying Amount	Fair Value	Carrying Amount	Fair Value
		(In thousands)		
Cash and cash equivalents	$ 66,708	$ 66,708	$ 23,443	$ 23,443
Net accounts receivable	419,479	419,479	400,005	400,005
Other current assets	74,964	74,964	54,070	54,070
Investments and other assets for which it is:				
Practicable to estimate fair value	184,487	185,679	149,645	150,170
Not practicable to estimate fair value	62,162	—	73,042	—
Short-term borrowings	333,185	333,185	279,305	279,305
Current portions of long-term debt and preference stock	280,772	280,772	146,969	146,969
Accounts payable	172,889	172,889	177,092	177,092
Other current liabilities	194,065	194,065	193,992	193,992
Long-term debt	2,758,769	2,767,721	2,598,254	2,694,858
Redeemable preference stock	134,500	141,621	242,000	254,809

Financial instruments included in other current assets include trading securities and miscellaneous loans receivable of the Constellation Companies. Financial instruments included in other current liabilities represent total current liabilities from the Consolidated Balance Sheets excluding short-term borrowings, current portions of long-term debt and preference stock, accounts payable, and accrued vacation costs. The carrying amount of current assets and current liabilities approximates fair value because of the short maturity of these instruments.

Investments and other assets include investments in common and preferred securities, which are classified as financial investments in the Consolidated Balance Sheets, and the nuclear decommissioning trust fund. The fair value of investments and other assets is based on quoted market prices where available. It was not practicable to estimate the fair value of the Constellation Companies' investments in several financial partnerships which invest in nonpublic debt and equity securities, investments in several partnerships which own solar powered energy production facilities, and in an investment in a company involved in the development of international power projects because the timing and magnitude of cash flows from these investments are difficult to predict. These investments are carried at their original cost in the Consolidated Balance Sheets.

The investments in financial partnerships totaled $48 million and $50 million at December 31, 1996 and 1995, respectively, representing ownership interests up to 10%. The aggregate assets of these partnerships totaled $6.1 billion at December 31, 1995. The investments in solar powered energy production facility partnerships totaled $11 million and $22 million at December 31, 1996 and 1995, respectively, representing ownership interests up to 12%. The aggregate assets of these partnerships totaled $35 million at December 31, 1995.

The fair value of fixed-rate long-term debt and redeemable preference stock is estimated using quoted market prices where available or by discounting remaining cash flows at the current market rate. The carrying amount of variable-rate long-term debt approximates fair value.

BGE and the Constellation Companies have loan guarantees on outstanding indebtedness totaling $21 million and $47 million, respectively, at December 31, 1996 and $22 million and $35 million, respectively, at December 31, 1995 for which it is not practicable to determine fair value. It is not anticipated that these loan guarantees will need to be funded.

Note 14. Quarterly Financial Data (Unaudited)

The following data are unaudited but, in the opinion of Management, include all adjustments necessary for a fair presentation. BGE's utility business is seasonal in nature with the peak sales periods generally occurring during the summer and winter months. Accordingly, comparisons among quarters of a year may not be indicative of overall trends and changes in operations.

	Quarter Ended				Year Ended
	March 31	June 30	September 30	December 31	December 31
	(In thousands, except per-share amounts)				
1996					
Revenues	**$861,330**	**$731,707**	**$825,960**	**$734,250**	**$3,153,247**
Income from operations	**201,315**	**148,637**	**275,667**	**43,846**	**669,465**
Net income	**100,781**	**64,553**	**146,482**	**(992)**	**310,824**
Earnings applicable to common stock	**91,118**	**52,448**	**137,862**	**(9,140)**	**272,288**
Earnings per share of common stock	**0.62**	**0.36**	**.93**	**(.06)**	**1.85**
1995					
Revenues	$717,806	$642,500	$848,781	$725,712	$2,934,799
Income from operations	148,222	120,920	299,744	126,806	695,692
Net income	70,854	50,889	163,335	52,929	338,007
Earnings applicable to common stock	60,902	40,937	153,104	42,486	297,429
Earnings per share of common stock	0.41	0.28	1.04	0.29	2.02

1996

Results for the second quarter reflect:

- *the $4.5 million after-tax write-off of disallowed replacement energy costs (see Note 1).*
- *the $14.6 million after-tax gain on the sale by a Constellation partnership of a power purchase agreement (see Note 3).*
- *the $7.0 million and $3.0 million after-tax write-offs by the Constellation Companies of the investment in two geothermal wholesale power generating plants and the development costs of a proposed coal-fired power project, respectively (see Note 3).*

Results for the third quarter reflect the $6.2 million after-tax write-off by the Constellation Companies of a portion of a solar power project investment (see Note 3).

Results for the fourth quarter reflect the $57.6 million after-tax write-off of disallowed replacement energy costs (see Note 1).

1995

Results for the third quarter reflect the $9.7 million after-tax write-off of certain Perryman costs (see Note 1).

Baltimore Gas and Electric Company

Directors

Christian H. Poindexter, 58
Chairman of the Board and
Chief Executive Officer, BGE

H. Furlong Baldwin, 65
Chairman of the Board and
Chief Executive Officer,
Mercantile Bankshares
Corporation

Beverly B. Byron, 64
Former Congresswoman,
U.S. House of Representatives

J. Owen Cole, 67
Chairman of the Board,
Blue Cross and Blue Shield
of Maryland, Inc.

Dan A. Colussy, 65
Chairman of the Board and
Chief Executive Officer,
UNC, Incorporated

Edward A. Crooke, 58
President and
Chief Operating Officer, BGE

James R. Curtiss, Esq., 43
Partner, Winston & Strawn

Jerome W. Geckle, 67
Retired Chairman of the Board,
PHH Corporation

Freeman A. Hrabowski III, 46
President, University of
Maryland, Baltimore County

Nancy Lampton, 54
Chairman and
Chief Executive Officer,
American Life and Accident
Insurance Company of Kentucky

George V. McGowan, 69
Former Chairman of the Board
and Chief Executive Officer, BGE

George L. Russell, Jr., Esq., 67
Partner, Piper & Marbury

Michael D. Sullivan, 57
Chairman of the Board,
Golf America Stores, Inc.

Officers

Christian H. Poindexter, 58
Chairman of the Board and
Chief Executive Officer

Edward A. Crooke, 58
President and
Chief Operating Officer

George C. Creel, 62
Executive Vice President and
Acting Chief Operating Officer

Robert E. Denton, 53
Senior Vice President, Generation

Thomas F. Brady, 47
Vice President, Customer Service
& Distribution

Charles H. Cruse, 52
Vice President, Nuclear Energy

Carserlo Doyle, 54
Vice President, Electric
Interconnection & Transmission

Jon M. Files, 61
Vice President,
Management Services

Frank O. Heintz, 52
Vice President, Gas

Sharon S. Hostetter, 52
Vice President,
Marketing & Sales

Ronald W. Lowman, 52
Vice President, Fossil Energy

G. Dowell Schwartz, Jr., 60
Vice President, General Services

Charles W. Shivery, 51
Vice President,
Finance & Accounting;
Chief Financial Officer and
Secretary

Joseph A. Tiernan, 58
Vice President, Corporate Affairs

Stephen F. Wood, 44
Vice President

Richard M. Bange, Jr., 52
Controller and
Assistant Secretary

Thomas E. Ruszin, Jr., 42
Treasurer and Assistant Secretary

John R. Collins, 39
Assistant Treasurer

Constellation Holdings, Inc.

Directors

Edward A. Crooke, 58
Chairman of the Board, Constellation Holdings; President and Chief Operating Officer, BGE

Bruce M. Ambler, 57
President and Chief Executive Officer, Constellation Holdings

H. Furlong Baldwin, 65
Chairman of the Board and Chief Executive Officer, Mercantile Bankshares Corporation

Roger W. Gale, 50
President, Washington International Energy Group

Jerome W. Geckle, 67
Retired Chairman of the Board, PHH Corporation

Edward W. Kay, 69
Retired Co-Chairman and Chief Operating Officer, Ernst & Young

George V. McGowan, 69
Former Chairman of the Board and Chief Executive Officer, BGE

Christian H. Poindexter, 58
Chairman of the Board and Chief Executive Officer, BGE

Mayo A. Shattuck III, 42
President and Chief Operating Officer, Alex. Brown, Inc.

Officers

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Chairman of the Board, Constellation Holdings

Bruce M. Ambler, 57
President and Chief Executive Officer, Constellation Holdings

Randall M. Griffin, 52
President, Constellation Real Estate Group

James W. Jeffcoat, 43
President, Constellation Health Services

Steven D. Kesler, 45
President, Constellation Investments

John F. Walter, 62
President, Constellation Power

Robert E. Windham, 54
President, Church Street Station

BGE Energy Projects & Services, Inc.

Officers

Edward A. Crooke, 58
Chairman of the Board

Stephen F. Wood, 44
President and Chief Executive Officer

BGE Home Products & Services, Inc.

Officers

Edward A. Crooke, 58
Chairman of the Board

William H. Munn, 49
President and Chief Executive Officer

Constellation Energy Source, Inc.

Officers

Edward A. Crooke, 58
Chairman of the Board and President

Changes in Officers and Directors

Effective January 1, 1996, George C. Creel, former Senior Vice President, Generation, was elected Executive Vice President. Mr. Creel also assumed the responsibilities of Chief Operating Officer until the completion of the merger. President and Chief Operating Officer Edward A. Crooke was assigned the responsibilities of co-chair of Constellation Energy Corporation's Transition Management Team, which guided all merger-related activities.

Effective January 1, 1997, Herbert D. Coss, Jr., retired from the company with more than 40 years of service. Frank O. Heintz replaced him as Vice President, Gas.

Effective January 31, 1997, Martin L. Grass resigned from BGE's Board of Directors due to time constraints associated with his responsibilities as Chairman and Chief Executive Officer of Rite Aid Corporation.

Five-Year Statistical Summary

	1996	1995	1994	1993	1992
Common Stock Data					
Quarterly Earnings Per Share					
First Quarter	$ .62	$ .41	$ .49	$ .38	$ .37
Second Quarter	.36	.28	.39	.31	.20
Third Quarter	.93	1.04	.79	1.01	.84
Fourth Quarter	(.06)	.29	.26	.14	.22
Total	$1.85	$2.02	$1.93	$1.85	$1.63
Dividends					
Dividends Declared Per Share	$1.59	$1.55	$1.51	$1.47	$1.43
Dividends Paid Per Share	1.58	1.54	1.50	1.46	1.42
Dividend Payout Ratio					
Reported	85.9%	76.7%	78.2%	79.5%	87.7%
Excluding disallowed replacement energy costs	70.0%	76.7%	78.2%	79.5%	87.7%
Market Prices					
High	$29¼	$ 29	$25½	$27½	$24⅜
Low	25	22	20½	22⅜	19¼
Close	26¾	28½	22⅛	25⅜	23⅜
Capital Structure					
Consolidated					
Long-Term Debt	45.0%	42.8%	46.1%	47.4%	46.1%
Short-Term Debt	5.0	4.4	1.0	—	0.2
Preferred and Preference Stock	6.5	8.5	8.9	9.2	9.8
Common Shareholders' Equity	43.5	44.3	44.0	43.4	43.9
Utility Only					
Long-Term Debt	42.5%	40.4%	43.6%	44.5%	42.9%
Short-Term Debt	6.1	5.2	1.2	—	0.3
Preferred and Preference Stock	7.8	10.0	10.5	10.9	11.6
Common Shareholders' Equity	43.6	44.4	44.7	44.6	45.2

The sum of the quarterly earnings per share amounts may not equal the total for the year due to changes in the average number of shares outstanding throughout the year.

The quarterly earnings per share amounts include certain one-time adjustments as shown in Note 14 to the Consolidated Financial Statements.

Common Stock Dividends and Price Ranges

	1996			1995		
	Dividend Declared	Price High	Price Low	Dividend Declared	Price High	Price Low
First Quarter	$ .39	$ 29½	$ 26⅛	$ .38	$ 25	$ 22
Second Quarter	.40	28⅝	25½	.39	26½	23⅛
Third Quarter	.40	28⅝	25	.39	26⅝	24⅜
Fourth Quarter	.40	28¾	25¾	.39	29	25½
Total	$ 1.59			$ 1.55		

Dividend Policy

The common stock is entitled to dividends when and as declared by the Board of Directors. There are no limitations in any indenture or other agreements on payment of dividends. Holders of preferred stock (first) and holders of preference stock (next), however, are entitled to receive, when and as declared from the surplus or net profits, cumulative yearly dividends at the fixed preferential rate specified for each series and no more, payable quarterly. They are also entitled to receive, when due, the applicable preference stock redemption payments before any dividend on the common stock shall be paid or set apart. Dividends have been paid on the common stock continuously since 1910. Future dividends depend upon future earnings, the financial condition of the company, and other factors. Quarterly dividends were declared on the common stock during 1996 and 1995 in the amounts shown above.

Common Stock Dividend Dates

Record dates are normally on the 10th of March, June, September, and December. Quarterly dividends are customarily mailed to each shareholder on or about the 1st of April, July, October, and January.

Dividend Reinvestment and Stock Purchase Plan

The company's Dividend Reinvestment and Stock Purchase Plan provides an opportunity for holders of the company's common stock to acquire additional shares of such stock in a convenient and economical manner. Participants in the plan may reinvest cash dividends on all or a portion of their shares of common stock and/or make optional cash payments.

Stock Trading

The company's common stock, which is traded under the ticker symbol BGE, is listed on the New York, Chicago, and Pacific stock exchanges, and has unlisted trading privileges on the Boston, Cincinnati, and Philadelphia exchanges. As of December 31, 1996, there were 77,550 common shareholders of record.

Transfer Agent and Registrar

Harris Trust and Savings Bank
Chicago, Illinois

Form 10-K

Upon written request, the company will furnish, without charge, a copy of its Form 10-K annual report, including financial statements, after it is filed with the Securities and Exchange Commission in March 1997. Requests should be addressed to Charles W. Shivery, Chief Financial Officer and Secretary, Vice President–Finance & Accounting, P. O. Box 1475, Baltimore, Maryland 21203-1475.

Auditors

Coopers & Lybrand L.L.P.

Executive Offices

Gas and Electric Building
Charles Center
Baltimore, Maryland 21201
Mail: P.O. Box 1475
Baltimore, Maryland 21203-1475

Shareholders' Inquiries and Assistance

Shareholders desiring assistance with lost or stolen stock certificates or dividend checks, name changes, address changes, stock transfers, or other matters should call the shareholder services representatives on our toll-free telephone numbers.

The following toll-free telephone numbers are available during our business hours, 8:00 a.m. to 4:45 p.m.:

Baltimore Metropolitan Area	(410) 783-5920
Within Maryland	1-800-492-2861
Outside of Maryland	1-800-258-0499

Letters should be addressed to:
Baltimore Gas and Electric Company
Shareholder Services
P.O. Box 1642
Baltimore, Maryland 21203-1642

BGE

P.O. Box 1475
Baltimore, Maryland 21203

www.bge.com