

**BEFORE THE PUBLIC SERVICE COMMISSION  
OF THE STATE OF DELAWARE**

IN THE MATTER OF THE APPLICATION                    )  
OF DELMARVA POWER & LIGHT COMPANY                )  
FOR A CHANGE IN THE GAS ENVIRONMENTAL            )       PSC DOCKET NO. 04-384  
SURCHARGE RIDER RATE                                )  
(FILED OCTOBER 1 2004)                                )

**ORDER NO. 6626**

**AND NOW**, to-wit, this 24th day of May, A.D., 2005;

**WHEREAS**, the Commission having received and considered the Findings and Recommendations of the Hearing Examiner ("Report") issued in the above-captioned docket, which was submitted after a duly noticed public evidentiary hearing;

**AND WHEREAS**, the Commission finds that the proposed increase in the Environmental Surcharge Rider as provided in the applicable tariff sheets of Delmarva Power & Light Company, d/b/a Conectiv Power Delivery, is just and reasonable and that its adoption is in the public interest; now, therefore,

**IT IS ORDERED:**

1. That by and in accordance with the affirmative vote of a majority of the Commissioners, the Commission hereby adopts the April 29, 2005 Findings and Recommendations of the Hearing Examiner, appended to the original hereof as "Attachment A."

2. That the Commission approves the Company's proposed rates and tariff changes, which reflect an increase in the environmental surcharge rider rate, as follows:

<u>Rate Schedules</u>	<u>Present Charge</u>	<u>Proposed Charge</u>
RG and GG	\$0.00044/Ccf	\$0.00083/Ccf
MVG & LVG	\$ 0.0044/Mcf	\$0.00827/Mcf
GVTF	\$0.00044/Ccf	\$0.00083/Ccf
MVFT, LVFT	\$ 0.0044/Mcf	\$0.00827/Mcf

3. That the Commission reserves the jurisdiction and authority to enter such further Orders in this matter as may be deemed necessary or proper.

BY ORDER OF THE COMMISSION:

\_\_\_\_\_  
Chair

\_\_\_\_\_  
/s/ Joshua M. Twilley  
Vice Chair

\_\_\_\_\_  
/s/ Joann T. Conaway  
Commissioner

\_\_\_\_\_  
/s/ Jaymes B. Lester  
Commissioner

\_\_\_\_\_  
/s/ Dallas Winslow  
Commissioner

ATTEST:

\_\_\_\_\_  
/s/ Karen J. Nickerson  
Secretary

A T T A C H M E N T "A"

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DELMARVA POWER & LIGHT COMPANY FOR A )  
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SURCHARGE RIDER RATE )  
(FILED OCTOBER 1, 2004) )

FINDINGS AND RECOMMENDATIONS OF THE HEARING EXAMINER

DATED: April 29, 2005

RUTH ANN PRICE  
HEARING EXAMINER

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**FINDINGS AND RECOMMENDATIONS OF THE HEARING EXAMINER**

Ruth Ann Price, duly appointed Hearing Examiner in this Docket pursuant to 26 *Del. C.* § 502 and 29 *Del. C.* ch. 101, by Commission Order No. 6493, dated October 19, 2004, reports to the Commission as follows:

**I. APPEARANCES**

On behalf of the Applicant, Delmarva Power & Light Company, d/b/a Conectiv Power Delivery ("Conectiv" or "the Company"):

TODD L. GOODMAN, ESQUIRE.

On behalf of the Public Service Commission Staff ("Staff"):

ASHBY & GEDDES  
BY: REGINA A. IORII, ESQUIRE.

On behalf of the Division of the Public Advocate ("DPA"):

G. ARTHUR PADMORE, PUBLIC ADVOCATE.

**II. BACKGROUND**

1. On October 1, 2004, Conectiv filed an application ("Application") with the Delaware Public Service Commission (the "Commission") seeking to increase its Environmental Surcharge Rider ("ESR") factor, effective on and after November 1, 2004, with

proration, and with such revised factors to continue in effect until October 31, 2005. The present approved rates and the proposed rates are as follows:

<u>Rate Schedules</u>	<u>Present Charge</u>	<u>Proposed Charge</u>
RG and GG	\$0.00044/Ccf	\$0.00083/Ccf
MVG & LVG	\$0.0044/Mcf	\$0.00827/Mcf
GVTF	\$0.00044/Ccf	\$0.00083/Ccf
MVFT, LVFT	\$0.0044/Mcf	\$0.00827/Mcf

According to the filing, under the proposed rates, the average residential heating customer using 120 Ccf a month during the winter heating season would experience an increase of \$0.05 or an increase of less than 0.1 percent since the last ESR filing.

2. In PSC Order No. 6493 (Oct. 19, 2004), the Commission allowed the new proposed Environmental Surcharge Rider to become effective on a temporary basis, subject to refund. In addition, the Commission designated Senior Hearing Examiner William F. O'Brien to conduct public evidentiary hearings and to report to the Commission his proposed findings and recommendations based on the evidence presented. Senior Hearing Examiner O'Brien delegated to me the task of conducting evidentiary hearings and preparing proposed findings and recommendations.

3. On October 29 and 30, 2004, the Company published notice of its Application which included information on how to intervene in the proceeding and announcing a public comment session on February 24, 2005. The Commission issued a press release on February 24, 2005

advising the public that the comment session scheduled for that day had been cancelled because of inclement weather. On March 2, 2005, the Company published notice of a public comment session to be held on March 31, 2005.

4. The Division of the Public Advocate made a timely notice to participate in the proceeding. No other party petitioned for intervention.

5. A duly noticed<sup>1</sup> public comment hearing was conducted on the evening of March 31, 2005, in Wilmington, Delaware. Public notice of the hearing included newspaper notice in the legal classified sections of the *Delaware State News* and *The News Journal* newspapers and direct notification by the Company of the organizations that participate in its "Project Concern" and ACORN. While several customers appeared at the public comment session, which was held jointly for this docket and for the Gas Cost Rate case, PSC Docket No. 04-301F<sup>2</sup>, no customer asked to speak at the session scheduled for consideration of the Environmental Rate Surcharge application or submitted written comments.

6. A duly noticed evidentiary hearing was conducted on April 4, 2005, in Wilmington. No members of the public attended the evidentiary hearing. The record, as developed at the hearing, consists of a 19-page verbatim transcript and four exhibits.

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<sup>1</sup>The affidavits of publication of notice from the *Delaware State News* and *The News Journal* are included in the record as Exhibit 1. Exhibits will be cited as "Ex.\_\_\_\_" and references to the hearing transcript will be cited as "Tr.\_\_\_\_."

<sup>2</sup>On October 1, 2004, Conectiv also filed an application for an increase in its Gas Cost Rate ("GCR"). The GCR case was captioned as In the Matter of the Application of Delmarva Power & Light Company, d/b/a Conectiv Power ... (footnote continued to next page.)

7. I have considered all of the record evidence and, based thereon, I submit for the Commission's consideration these findings and recommendations.

### **III. SUMMARY OF THE EVIDENCE**

8. **Company's Direct Testimony.** Conectiv submitted the pre-filed testimony of one witness, Heather G. Hall, Regulatory Affairs Lead. Ms. Hall provided the overview for Conectiv's case and summarized the proposals and rationale for those proposals. Ex. 2. Ms. Hall explained that by Order No. 6401 (Apr. 20, 2004), the Commission approved the environmental surcharge rider that placed into effect the current rate of \$0.00044 per Ccf. As stated by Ms. Hall, the purpose of the Environmental Surcharge Rider is to allow the Company to recover certain expenses associated with remediation of its Manufactured Gas Plant sites. Ex. 2 at 3.

9. In the instant application, filed on October 1, 2004, the Company seeks to increase the Environmental Surcharge Rate from \$0.00044 per Ccf to \$0.00083 per Ccf based upon the \$55,751 in expenses incurred during the Environmental Cost Year of June 1, 2003 through May 31, 2004. Ex. 2 at 2, 4. Approval of the Company's request for space heating customers would increase by \$0.05 or less than one percent (1%). Ratepayers would experience an increase from \$130.23 to \$130.28 in their bills. Ex. 2 at 12.

10. According to the Department of Natural Resources and Environmental Control ("DNREC") designations, the Company has four manufactured gas plant sites in Delaware. There are three sites

located in Wilmington - Wilmington Coal Gas Site North, Wilmington Coal Gas Site South, and Wilmington Public Works Yard. The fourth site is located in New Castle. Ex. 2 at 10.

11. The costs requested to be recovered in the Company's filing are the Feasibility Study and Remediation Plan for the Wilmington Coal Gas Site North. Ex. 2 at 11.

12. Public notice of the proposed remedy for the site was filed during August 2004. After receiving no comments from the public during the twenty (20) day comment period, DNREC approved the Company's Remediation Plan and construction to implement the remedy which will occur during the June 2004 through May 2005 Environmental Cost Year.<sup>3</sup>

13. The environmental cost year is defined as "the time period over which environmental costs are incurred and any payment from other parties are netted against those costs." Ex. 2 at 4.

14. The costs claimed by the Company are \$55,751 that represent some legal expenses, but, primarily, these costs are payments made to engineering and consulting companies that assisted the Company in its remediation of Manufactured Gas Plant sites. These firms perform various tasks such as ground water testing and work plan development. Ex. 2 at 5.

15. The Environmental Cost Year of June 1, 2003 through May 31, 2004 will recover expenses in the amount of \$55,751 (Ex. 2 at 4)

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<sup>3</sup>Company witness, Heather G. Hall, noted that the Company intends to file for recovery of out-of-pocket expenses associated with its remediation activities for the Wilmington Public Works Yard for the period of June 1, 2004 through May 31, 2005. Ex. 2 at 11. Further, during the same cost year, the Company anticipates filing for recovery of the costs associated with the remedial investigation, feasibility study, and proposed remedy for that site. Ex. 2 at 11.

during the recovery period of November 1, 2004 through October 21, 2005 (*Id.* at 7).

16. The Company's tariff sheet No. 79 defines the costs eligible for recovery by this rider as "[a]pplicable environmental costs are those incurred as a result of, but are not limited to, investigating, testing, monitoring, remediation, land acquisition, legal costs related directly to the site remediation, and disposal sites. The costs must be actually incurred, incremental "out-of-pocket" remediation related expenses, and must exclude such costs as internal labor and overhead expenses." Ex. 2 at 5.

17. Ms. Hall explained the process for calculating the environmental surcharge as: The amount of eligible environmental costs, \$55,751, is amortized over a five-year period, offset with the deferred tax benefit to customers. Ex. 2 at 8 and Schedule HGH-2. Therefore, for the recovery year beginning November 1, 2004, the amount of \$9,122.85 will be recovered under this Application. *Id.*

18. Ms. Hall observed that the reconciliation factor applicable in this case accounts for an unusual amount of under-collection in the preceding recovery period necessitated by the fact that the environmental surcharge rider went into effect on April 13, 2004 rather than November 1, 2003.<sup>4</sup>

19. The reconciliation factor is the amount actually over-collected or under-collected from customers for the twelve-month

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<sup>4</sup>The Commission entered Order No. 6401 (Apr. 20, 2004) (in PSC Docket No. 04-53) in which it approved Conectiv's environmental surcharge of \$522,988. Conectiv filed its application on February 13, 2004 for recovery of the amount of \$522,988 based on actual costs and forecasted sales data. It was determined that after the initial year the calculation would be based on a twelve month period. However, for Year 1, the calculation would be based upon six and one-half months of costs prorated over twelve months. Ex. 2 at 8-9.

period ending with the month of July immediately preceding the beginning of the next recovery year. Ex. 2 at 7.

20. As shown in the Schedule of Over/Under Collection (Schedule HGH-3) appended to Ms. Hall's pre-filed testimony, since the environmental rider went into effect on April 13, 2004, the months of November 2003 through March 2004 show no recovery. Ex.2 at 8. In order to avoid burdening customers with an abnormally high surcharge that collected all of the initial environmental surcharge in one year, the initial surcharge was calculated as if it had been in effect for twelve months even though it was in effect only six and one-half months.<sup>5</sup>

21. The initial recovery period resulted in an unusually high under-collection because the rate went into effect in April 2004 rather than November 2003. Id. Accordingly, the under-collected amount of \$63,525.37 is the reconciliation factor. Ex.2 at 9. This amount is approximately thirty-nine percent (39%) of the proposed increase in this case. Id.

22. The environmental surcharge rider proposed in this case (an increase of \$0.00083 per Ccf) seeks a net recovery amount of \$162,982.12 for the recovery year beginning November 1, 2004 and ending October 31, 2005, calculated on the environmental cost year of June 1, 2003 through May 31, 2004. The net recovery amount includes the following factors:

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<sup>5</sup>In PSC Docket No. 04-53, the Commission ordered (pursuant to Order No. 6401) an initial environmental surcharge of \$475,442.23 that was amortized over five years. Under the amortization schedule, the amount of \$85,579.33 was scheduled to be collected from ratepayers in the first year. Since the surcharge was approved in April 2004, leaving only six and one-half months for this amount to be recovered, the Commission avoided ratepayer "sticker shock" by deferring the amount of \$63,525.37 to the second year.

\$90,333.90:	Second Year Amortization for Initial ESR ordered in PSC Docket No. 04-53
\$ 9,122.85:	First Year Amortization for costs of \$55,751.10 for this Application
\$ 3,525.37:	Under-collection from customers from November 2003 through August 2004
<hr/>	
\$162,982.12	Net recovery amount

23. The proposed rate of \$0.00827 per Mcf or \$0.00083 per Ccf is derived by dividing the net recovery amount of \$162,982.12 by the projected firm sales of 19, 737,672 Mcf for the recovery year. Ex. 2, HGH-5.

24. **Staff's Direct Testimony.** Mary E. Paskey, a Public Utilities Analyst for the Delaware Public Utilities Commission, provided Staff's position regarding the proposed increase to the environmental surcharge rider. Ex. 4.

25. Ms. Paskey reported that the Commission's Staff conducted a thorough audit of all of the Company's expenses to verify the level of environmental expenses eligible for recovery. Ex. 4 at 3. The audit included all of the Company's invoices for the twelve-month period from June 1, 2003 through May 31, 2004 for the Wilmington Coal Gas Site-North.<sup>6</sup> Ex. 4 at 4.

26. The audited accounts are used to track out-of-pocket expenses, such as consulting, legal, and other expenses related to the remediation process. *Id.*

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<sup>6</sup>Conectiv's books contain two accounts numbered 5227094 and 5227095 that include expenses, such as legal, consulting and other, for the Wilmington Coal Gas Site-North. Ex. 3, Schedule-MEP-2.

27. Staff found no variances between the Company's claimed expenses for environmental costs and those subjected to audit. Id.

28. Of concern to Staff, however, were the markup fees charged by vendors and subcontractors to the Company. Ex. 4 at 4. As an example, Ms. Paskey noted that one vendor charged a mark-up fee of five percent (5%) for other direct costs, but the vendor's subcontractor also charged a ten percent (10%) markup fee. Id. Therefore, two markup fees totaling fifteen percent (15%) would be passed onto the ratepayers. Id. In another instance, Ms. Paskey found that one subcontractor was charging an eight per cent (8%) markup; an amount that was two percent (2%) above the Master Agreement rate. Ex. 4 at 4-5.

29. Ms. Paskey acknowledged that the Company had worked diligently to obtain discounted rates for markup fees. Ex. at 5. She noted that the Company responded to a data request that the average markup for the industry was 5% to 15% but the markup range for the Wilmington Coal Gas Site-North project was 3% to 8%. Id. Ms. Paskey questioned, "why is the Company allowing, not only a markup on a markup but also allowing a total markup that is well above the range for this particular project?" Ex.4 at 5.

30. Although the amount of the markup for this case was insignificant, Staff recommended that "the Company in the future not be allowed to recover the markup expense a vendor incurs as a result of having to hire a subcontractor to complete a project on which they bid." Ex. 4 at 6.

31. With regard to the instant Application, Staff found that the Company's calculations were correct and the rate requested was appropriate. Id. Therefore, Staff recommended approval of the

increase in the Environmental Rate Rider from \$0.00044 per Ccf to \$0.00083 per Ccf. Ex. 4 at 7.

32. **Company's Rebuttal Testimony.** The Company pre-filed the rebuttal testimony of Philip L. Phillips, Jr., to defend solely the portion of Staff's testimony relating to the markups charged by both the Company's vendor and subcontractor. Ex. 3 at 2. Mr. Phillips is an engineer who has been employed at Conectiv since 1970. Ex. 3 at 1.

33. Mr. Phillips did not appear at the evidentiary hearing, but his testimony was admitted into evidence without objection after it was adopted by Ms. Hall.<sup>7</sup> Tr. 35-36.

34. Ms. Hall's pre-filed rebuttal testimony argues that markup expenses, as those claimed by the Company in this case, are "reasonable and legitimate out-of-pocket business expenses that the Company should be permitted to recover." Ex. 3 at 3. Ms. Hall contended the Company's tariff sheets, approved by the Commission, specified the types of costs that could be recovered under the environmental surcharge rider. Id. Ms. Hall cited Tariff Leaf No. 79 which provides:

Applicable environmental costs are those incurred as a result of, but are not limited to, investigating, testing, monitoring, remediation, land acquisition, legal costs related directly to the site remediation, and disposal sites. These costs must actually be incurred, incremental "out-of-pocket" remediation related expenses and must include such costs as internal labor and overhead expenses.

Id. at 4.

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<sup>7</sup>Since the Company's prefiled rebuttal testimony was not sworn to by its author, Philip L. Phillips, Jr., at the evidentiary hearing, he will not be referred to as its sponsor. Tr. 34-35. At the evidentiary hearing, Heather Hall adopted Mr. Phillips testimony as her own; therefore, the Company's rebuttal testimony will be referred to as that of Ms. Hall. Tr. 35-36.

35. Ms. Hall characterized markup fees charged by a vendor as "a percentage which is added to the costs of a particular activity to cover administrative costs associate[d] with the activity" Id. at 5. According to Ms. Hall, such fees cover expenses for tracking time spent on a project and ministerial activities such as photocopying and computer charges. Id.

36. Specifically, Ms. Hall relies on the tariff language that the administrative markup costs are "incurred as a result of ... investigating, testing, etc." These costs are "actually incurred" out-of-pocket expenses; therefore, these costs are properly recoverable in the environmental rate surcharge. Id. at 4.

37. Further, Ms. Hall asserted that Staff accepts the markup fee that a vendor charges for its own administrative costs, but Staff objects to the markup fee that a subcontractor charges the vendor for the subcontractor's administrative costs. Id. at 5. Ms. Hall remarked that a subcontractor, like the vendor, has its own administrative costs that are legitimately incurred in the subcontractor's performance of the work. These costs would not be any less if the actual work were performed by a vendor or by a subcontractor. Id.

38. Ms. Hall contends that the administrative costs are not additional costs charged to a project, but rather, these costs are costs associated with the actual work performed while completing the project by either the vendor or the subcontractor. Further, Ms. Hall explained that subcontractors are used because they often have specific expertise and the ability to efficiently handle a discrete portion of work to be done which decreases the costs of the project to the Company. Ex. 4 at 8.

39. Further, Ms. Hall observed that the costs of a project, including the billing methodology, are usually included in the price bid for the project. Id. The Company continually monitors the ongoing work of the project, including the costs incurred by the vendor or subcontractor and the billing methodology. Since the costs are reasonable and incurred in the actual performance of the work, Ms. Hall contended they are appropriately recoverable expenses. Id.

#### **IV. DISCUSSION**

##### **A. Uncontested Matters That Require Commission Action**

40. The Company and Staff agree that the Environmental Surcharge Rider should be increased from the currently effective rate of \$0.00044 per Ccf to \$0.00083 per Ccf. Both the Company and Staff have meticulously reviewed the expenses in the accounts related to the Wilmington Coal Gas Site, and the parties agree that the expenses are reasonable and appropriate.

41. Moreover, I find that the average residential heating customer using 120 Ccf a month during the winter heating season would experience a small increase of \$0.05 or an increase of less than 0.1 percent in their heating bill due to this increase.

42. Accordingly, I recommend that the Commission approve the Company's application for an increase in the Environmental Surcharge Rider Rate as stated in its Application and accompanying proposed tariffs.

**B. The Sole Contested Matter - Administrative Markup Costs**

43. At the outset, I note that for this Application alone, the Company and Staff agree that the markups included in the audited accounts for vendor and subcontractor markup costs are not in dispute.

44. In this case, at issue was a subcontractor's markup of sixty-nine cents (\$0.69). Tr. 47. This amount was passed on to the vendor who added five percent (5%) to its bill as an administrative markup for a total administrative markup of \$7.57. Id.

45. The parties have agreed to review and discuss this issue prior to the Company's next environmental cost rate rider filing. Finally, the Company and Staff have agreed to meet informally to discuss ways to resolve this issue.

**V. RECOMMENDATIONS**

In summary, and for the reasons discussed above, I propose and recommend to the Commission that it approve as just and reasonable the Company's proposed Environmental Surcharge Rider Rate from \$0.00044 per Ccf to \$0.00083 per Ccf.

Respectfully submitted,

/s/ Ruth Ann Price  
Ruth Ann Price  
Hearing Examiner

Dated: April 29, 2005