

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

IN THE MATTER OF THE APPLICATION OF)
DELMARVA POWER & LIGHT COMPANY FOR)
APPROVAL TO MODIFY ITS STANDARD OFFER)
SERVICE SUPPLY RATE TO REFLECT A) PSC DOCKET NO. 09-9
REVISION TO THE REASONABLE ALLOWANCE)
FOR A RETAIL MARGIN ("RARM"), PURSUANT)
TO PSC DOCKET NO. 04-391)
(FILED JANUARY 6, 2009))

ORDER NO. 7703

This 22nd day of December, 2009, the Commission determines and Orders the following:

WHEREAS, on January 6, 2009, Delmarva Power & Light Company ("Delmarva" or the "Company") having filed an application with the Commission seeking approval to increase its Reasonable Allowance For Retail Margin ("RARM") in its Standard Offer Service ("SOS) supply rate, pursuant to the regime approved in PSC Order No. 6746 (October 11, 2005) in PSC Docket No. 04-391;

WHEREAS, by Commission Order No. 7603 (July 7, 2009) the Commission referred the matter to this Hearing Examiner for the purpose of conducting a public comment session and evidentiary hearings, and summarizing any testimony presented at such hearings;

WHEREAS, this Hearing Examiner held an evidentiary hearing and public comment session in Dover, Delaware on Monday, November 23, 2009.

WHEREAS, the Commission has received and considered the Findings and Recommendations of the Hearing Examiner issued in the above captioned-Docket, which was submitted after a duly-noticed public

evidentiary hearing, and which is attached to the original hereof as Attachment "A";

AND WHEREAS, the Hearing Examiner recommends that the Reasonable Allowance for Retail Margin ("RARM") proposed by Delmarva Power & Light Company ("Company") in its January 6, 2009 application and its January 29, 2009 supplement be approved as just and reasonable for services rendered on and after March 2, 2009.

AND WHEREAS, according to the filing, under the proposed RARM, the average residential customer using 1,000 kWh per month would experience an increase of \$0.32 or 0.2 percent.

AND WHEREAS, the Hearing Examiner recommends that the Proposed Settlement Agreement dated October 29, 2009, which was endorsed by all the parties, and which is attached to the original hereof as Attachment "B", be approved as reasonable and in the public interest;

NOW, THEREFORE, IT IS HEREBY ORDERED BY THE AFFIRMATIVE VOTE OF NOT FEWER THAN THREE COMMISSIONERS:

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

2. That the Commission approves the Proposed Settlement, appended to the original hereof as Attachment "B" and Delmarva Power & Light Company's proposed Reasonable Allowance for Retail Margin.

3. That the Reasonable Allowance for Retail Margin approved by the Commission in Order 7531 (February 5, 2009) is hereby approved. This shall be effective on or after March 2, 2009.

4. That the Commission approve the requested modifications to the Company's Tariffs reflecting the increase sought in the Company's application. These modifications are contained in the proposed Tariffs filed by the Company on January 6, 2009 and January 29, 2009.

5. 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:

/s/ Arnetta McRae
Chair

/s/ Joann T. Conaway
Commissioner

/s/ Jaymes B. Lester
Commissioner

/s/ Dallas Winslow
Commissioner

/s/ Jeffrey J. Clark
Commissioner

ATTEST:

/s/ Alisa Carrow Bentley
Secretary

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

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FINDINGS & RECOMMENDATIONS OF THE HEARING EXAMINER

DATED: December 8, 2009

MARK LAWRENCE
HEARING EXAMINER

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FINDINGS AND RECOMMENDATIONS OF THE HEARING EXAMINER

Mark Lawrence, duly appointed Hearing Examiner in this Docket, pursuant to 26 *Del. C.* § 502 and 29 *Del. C.* ch. 101, by the Commission's Order No. 7531 dated February 5, 2009 and the Commission's Order No. 7603 dated July 7, 2009, reports to the Commission as follows:

I. APPEARANCES

On behalf of Delmarva Power & Light Company ("Delmarva" or "Company")

BY: TODD GOODMAN, ESQ., ASSISTANT GENERAL COUNSEL
 A. Glenn Simpson, Mgr., Regulatory Compliance Pricing
 Heather Hall, Manager, Delaware Regulatory Affairs,
 External Issues & Compliance
 Gary Cohen, Mgr., Regulatory Affairs, External Issues
 Leonard J. Beck, Senior Regulatory Affairs Analyst

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

BY: JOSEPH HANDLON, ESQ., DEPUTY ATTORNEY GENERAL, PSC
 Pamela R. Knotts, Public Utilities Analyst
 John Farber, Public Utilities Analyst

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

BY: KENT WALKER, ESQ., DEPUTY ATTORNEY GENERAL
 G. Arthur Padmore, Public Advocate
 Michael D. Sheehy, Deputy Director, Public Advocate

II. BACKGROUND

1. In PSC Order No. 6746 (Oct. 11, 2005), in PSC Docket No. 04-391, the Delaware Public Service Commission ("the Commission") approved a Settlement Agreement ("Settlement") allowing Delmarva Power & Light Company ("Delmarva" or the "Company") to recover, in its Standard Offer Service ("SOS") supply rate, a "reasonable allowance for retail margin" ("RARM"), which includes recovery of the incremental expenses Delmarva incurs in providing fixed price SOS and Hourly Priced Service (HPS) and \$2.75 million per year.¹ (See PSC Order No. 6746, p. 10.) The parties' Settlement required that Delmarva submit, "approximately four months after the start of Year 2" of the SOS procurement process, an application to revise its rates to reflect a true-up of actual RARM costs incurred up to the end of Year 1. Additionally, the Application was to include a re-setting of the millage rate charged to fixed price SOS customers to collect the \$2.75 million portion of the RARM based on actual collections during Year 1.

2. On December 27, 2007, Delmarva filed its Year 2 application in PSC Docket No. 07-364, seeking to increase the RARM established in PSC Docket No. 04-391 to reflect the actual year 1 SOS costs it incurred from May 1, 2006 to May 31, 2007. The Commission approved the Year 2 increased RARM in PSC Order No. 7406 (June 17, 2008).²

¹ At the time the Commission approved the Settlement, the "Electric Utility Restructuring Act of 1999" directed DPL to include in its SOS rates a "reasonable allowance for retail margin to be determined by the Commission." (See 26 Del. C. § 1006(a) (2) (c), prior to 2006 amendments.) With the "Electric Utility Supply Act of 2006," the Delaware General Assembly amended § 1006 and, among other things, deleted the reference to RARM. While there is no longer any specific statutory requirement for SOS to include a RARM, § 1007 (c) (1) (a) of the Electric Utility Supply Act of 2006 cites the SOS "procurement process approved in PSC Docket No. 04-391" as comprising a portion of the SOS resource mix, which includes collection of the RARM.

3 On January 6, 2009, the Company filed its Year 3 Application for the SOS Year ending May 31, 2008. Delmarva's Application seeks to increase the RARM charge in the amount of \$0.32 or 0.2%, per month, for an average residential customer using 1,000 kWh. However, Staff noted that the proposed RARM charge results in an increase of approximately 13.60% over the Year 1 RARM charge approved in Docket 07-364. (See Knotts, Exhibit 5, p.3, LL 19-21.)

4. On February 5, 2009, the Commission entered PSC Order No. 7531 in this Docket, which approved the proposed increase on a temporary basis, subject to refund with interest, with an effective date of March 2, 2009. (See PSC Order No. 7531, Para. 7.) This Order also required the publication of public notice of the proposed increase and a deadline by which comments concerning the proposed increase would be filed. On July 7, 2009, the Commission entered PSC Order No. 7603 assigning Mark Lawrence as the Hearing Examiner and giving him the authority to conduct an evidentiary hearing. The public notice was published in The Delaware State News on August 10, 2009, and in The Sussex Post and The News Journal on August 13, 2009. No written comments were received by the September 1, 2009 deadline contained in the public notice. (See Knotts, Exhibit 5, p.5, LL 16-18.) On July 30, 2009, the Division of the Public Advocate (DPA) filed its Notice of Intervention. No other Petitions of Intervention were filed.

5. The parties conducted a workshop on August 4, 2009 and a meeting on September 9, 2009, attempting to resolve the issues in this Docket. The Hearing Examiner continued the September 15, 2009

Evidentiary Hearing/Public Comment Session based upon the parties' request due to promising settlement discussions. The Evidentiary Hearing/Public Comment Session was held on Monday, November 23, 2009 at 10 a.m. at the Commission's office in Dover, Delaware. No members of the public attended the Evidentiary Hearing/Public Comment Session. Notice of the Evidentiary Hearing/Public Comment Session was published in The Delaware State News and The News Journal on October 23, 2009, and in The Sussex Post on October 29, 2009. (See composite Exhibit "1" from 11/23/09 Evidentiary Hearing/Public Comment Session and continued 9/15/09 Hearing, including Public Notices of Hearing & Affidavits of Publication.)

6. At the evidentiary hearing on November 23, 2009, Delmarva requested that the Commission approve an increase in its Reasonable Allowance for Retail Margin ("RARM"). Delmarva filed its Application on January 6, 2009 and amended its Application on January 29, 2009. (See Composite Exhibit "2" hereinafter "the Application.") The revised Tariff sheets proposed by Delmarva are attached thereto. (*Id.*)

7. Delmarva's Application was filed pursuant to PSC Order No. 6746 (Oct. 11, 2005) in Docket No. 04-391. (See Delmarva's Application Filing Letter docketed Jan. 6, 2009.) PSC Order No. 6746 approved the parties' Settlement Agreement dated July 14, 2005. (See Exh. 2, Section G, Parts 3 & 4, pp 15-16.)

8. Delmarva's current Application proposed an increase with usage (without proration) effective on the electric customer's first bill cycle in March 2009. (See Tariffs attached to Application.) Delmarva's Application stated that "[t]he impact to an average

residential customer using 1,000 kWh is \$0.32 per month, or an increase of 0.2%." The new RARM factor proposed in the Application is \$.0027727/kWh. (See Delmarva's Filing Letter docketed Jan. 6, 2009.) Delmarva's attached its RARM calculations to its Application. Delmarva's "Delaware SOS RARM True-Up Calculation" reflecting costs through May 31, 2008 was also admitted into evidence at the evidentiary hearing. (See Exh. "2A.") Before examining the additional evidence submitted by Delmarva and the PSC Staff, however, a brief description of RARM is necessary.

9. According to the Settlement Agreement incorporated in PSC Order No. 6746 (Oct. 11, 2005), the RARM consists of:

"a) incremental expenses incurred: **i**) to provide Fixed Price-Standard Offer Service ("FP-SOS") and Hourly Priced Service ("HPS"); **ii**) to administer the Volumetric Risk Mitigation (VRM) mechanism described below and applicable with respect to FP-SOS customer load; and **iii**) carrying costs on Cash Working Capital (CWC) for FP-SOS and HPS; **b**) \$2.75 million per 12 month period, which, for the Year 1 and 2 rates,² is deemed to include any carrying costs on incremental capitalized costs associated with providing FP-SOS and the VRM mechanism, but does not include the separately calculated carrying costs for capitalized billing system software costs needed to bill and track HPS costs and revenues and also does not include any return on investment that is removed from distribution rates as supply related; **and c**) for GS-T customers and those in the GS-P class that have made an election for HPS, the allocable share of the above categories plus an amortized amount, including carrying costs on the unamortized balance of the capitalized billing system software costs and interface systems needed to bill and track HPS costs and revenues." (See Settlement Agreement in PSC Order No. 6746, Section D (4))

² Pursuant to Section II A of the 2005 Settlement Agreement, "Year 1" is defined as the 13-month period of May 1, 2006 - May 31, 2007 and "Year 2" is defined as the period of June 1, 2007 - May 31, 2008. Subsequent "Years" are defined as June 1st of the calendar year through May 31st of the following calendar year.

III. SUMMARY OF THE EVIDENCE.

A. Company's Pre-Filed Testimony

10. On November 10, 2009, the Company filed the pre-filed testimony of A. Glenn Simpson, the Manager of Regulatory Compliance Pricing. Mr. Simpson testified that Delmarva is permitted to recover, in its Standard Offer Service ("SOS") supply rate, a reasonable allowance for retail margin ("RARM"), which includes recovery of the "incremental expenses" Delmarva incurs in providing fixed price SOS and Hourly Priced Service (HPS) and \$2.75 million per year. (Exh. 3, p. 2, LL 10-13)

11. Mr. Simpson testified that the "incremental expenses" are "defined to include the Cash Working Capital (CWC) to provide SOS ... Incremental expenses that are recovered through the RARM include Estimated Annual Ongoing Costs, Net Uncollectables and other taxes, Amortization of Implementation Costs, Amortization of Prior Year Under or Over-Collections and Cash Working Capital." (Exh. 3, p. 2, LL 18-21)

12. Mr. Simpson testified that Delmarva's current Application "included a breakdown of implementation and ongoing costs by year, the amortization schedules for under-collected implementation, Year 1, and Year 2 costs, a breakdown of estimated on-going annual costs, a detail of the margin collected and actual kWh sales by month and customer type, a copy of the SOS pricing model with the proposed RARM rate, bill comparison calculations for summer, winter, and total

bills by customer class, and calculation of the RARM for HPS customers with corresponding detail." (Exh. 3, p. 3, LL 10-16)

13. According to Mr. Simpson, in agreeing to the proposed Settlement Agreement, Delmarva "had agreed to four adjustments to the costs as shown in Delmarva's application: 1) the provision for collecting the City of Wilmington franchise tax was over-collected and the Company agreed to reduce the requested amount by \$609,505; 2) invoices for a contractor included a provision for Company facilities in the amount of \$1,664, which the Company agreed to remove from its application; 3) the summary of costs overlooked two items and the parties agreed to increase the requested amount by \$7,017 to allow this correction; and 4) the parties agreed to reduce the Rate of Return (ROR) for the amortization of the Year 2 under-collected amounts from the 10.49% ROR allowed in the Company's last rate case to 6.4%. This had the effect of reducing the annual requirement from \$256,160 to \$232,681, a difference of \$23,490 per year." (Exh. 3, p. 3, LL 22-23, p. 4, LL 1-9)

14. By agreeing to the Settlement Agreement, Delmarva also agreed that, in Year 3 ending May 31, 2009, the Company shall be permitted to recover the actual uncollectible SOS supply and transmission-related expense, not to exceed \$7,280,767. Thus, the parties agreed to temporarily impose a cap on an expense category which has recently been increasing. (Exh. 3, p.4, LL 10-13 & p.5, LL 8-11)

15. In Year 4 ending May 31, 2010 and subsequent years, the RARM uncollectible expense shall be the actual uncollectible SOS

related expense for a three (3) year normalized average ending with the period covered by the application. (See Ex. 3, p. 4, LL 13-15 & Exh. 4, Settlement Agreement, Para. 5 and Exh."A" thereto, Para. 5.)

16. In Year 4 and subsequent years, the parties also agreed that, unless the total RARM costs increases or decreases by at least 5.25%, the allowed RARM total costs will not change from year-to-year. (See Exh. 3, p. 4, LL 10-18 & p.5, LL & Exh. 4, Settlement Agreement, Para. 6 and Exh. "A" thereto, Para. 6) According to Mr. Simpson, this "helps promote stability to the RARM rate while allowing the company to recover its costs if collections get too far out of sync with costs." (Exh. 3, p. 5, LL 16-17) In Year 4 and subsequent years, if the 5.25% threshold is not exceeded, the Company is required to provide a RARM True-Up calculation and additional information for the test period. (See Settlement Agreement, Para.7 and Exh."A" thereto, Para. 7) The Settlement Agreement allows the Company to recover the difference between the total RARM Cost actually recovered during the test period and the total RARM Cost that was last approved by the Commission, plus interest in the proposed RARM cost. (Exh.3, p.6, LL 11-14 & Settlement Agreement, Exh. 4, Para. 8 and Exh. "A" thereto, Para. 8)

17. In Year 4 ending May 31, 2010 and subsequent years, if the 5.25% threshold is not exceeded in either direction for three (3) consecutive years, the threshold may be reevaluated by the parties to determine if a more appropriate threshold should be applied. (Ex. 3, p. 6, LL 9-11 & Settlement Agreement, Para. 7)

B. Staff's Pre-Filed Testimony

18. **Testimony of Pamela R. Knotts.** On November 16, 2009, Staff filed the pre-filed Testimony of Public Utilities Analyst, Pamela R. Knotts.

19. As to the Company's Application, Ms. Knotts also testified that the City of Wilmington franchise tax was over-collected. The Company had agreed to reduce the requested amount by \$609,505. (Knotts, Ex. 5, p. 5, LL 21-23) Also, invoices for a contractor included a provision for Company facilities in the amount of \$1,664, which the Company agreed to remove from its application. (Knotts, Ex. 5, p.6, LL 7-9). Lastly, the summary of costs overlooked two items and the parties agreed to increase the requested amount by \$7,017 to allow this correction. (Knotts, Ex. 5, p. 7, LL 7-9) Staff audited more than \$1 million dollars of invoices relating to the Year 2 Incremental Costs. (See Knotts, Exhibit 5, p.5, LL 5-8.)

20. The Company's "uncollectable expense" had increased by 102% and the Company was calculating a dollar-for dollar recovery. (Knotts, Ex. 5, p.6, LL 10-12). According to the PSC's former Regulatory Policy Administrator (now Deputy Director), Janis Dillard, "the level of uncollectable expense to be recovered in the RARM was not intended to change on an annual basis to give the Company protection against the risk of uncollectables. (Knotts, Ex. 5, p.6, LL 12-18). Rather, "it was seen as mirroring the uncollectable policy in base rates and the Company could file for a change in the RARM to reflect any changes approved by the Commission in base rates." (Knotts, Ex. 5, p.6, LL 18-21).

21. Ms. Knotts also testified that the parties agreed to reduce the Rate of Return (ROR) for the amortization of the Year 2 under-collected amount from the 10.49% ROR allowed in the Company's last rate case to 6.4%. (Knotts, Ex. 5, p. 6, LL 22-25, p. 7, LL 1-2). The Company had argued that the same amortization for Year 2 should be used for Year 1. (Knotts, Ex. 5, p.9, LL 9-11). The 6.4% carrying cost on under-collection of \$2,173,578 from Year 2 will be amortized over five (5) years. This 6.4% represents a debt rate which Delmarva used to issue certain five (5) year bonds. (Knotts, Ex. 5, p.10, LL 17-20). This had the effect of reducing the annual requirement from \$256,160 to \$232,681, a difference of \$23,490 per year." (Simpson, Exh. 3, p. 3, LL 22-23, p. 4, LL 1-9).

22. By agreeing to the Settlement Agreement, Staff and Delmarva also agreed that, in Year 2, the Company shall be permitted to recover the actual supply and transmission-related costs of uncollectible SOS expense, not to exceed \$6,290,040. According to Ms. Knotts, this figure included the Year 2 RARM factor approved by the Commission in Order 7406 except that a \$0.000027/kWh increase was recognized. (Knotts, Ex. 5, p.10, LL 1-2 & FN 9). Thus, "the approved RARM factor for Year 2 included the required recovery of Year 1 under-collection of Total RARM cost, plus other RARM cost components." (Knotts, Ex. 5, p. 10, LL 3-5)

23. For Year 3, the Company shall be permitted to recover the actual supply and transmission-related costs of uncollectible SOS expense, not to exceed \$7,280,767. (Knotts, Ex. 5, p.8, LL 9-20).

24. In Year 4 ending May 31, 2010 and subsequent years, the RARM uncollectible expense shall be the actual uncollectible SOS related expense for a three (3) year normalized average ending with the period covered by the application. (See Ex. 3, p.4, LL 13-15 & Exh. 4, Settlement Agreement, Para. 5 and Exh. "A" thereto, Para. 5.)

25. In Year 4 and subsequent years, the parties also agreed that, unless the total RARM costs increases or decreases by greater than 5.25%, the allowed RARM total costs will not change from year-to-year. (See Knotts, Exh. 5, p. 10, LL 8-16 & p.5, LL & Exh. 4, Settlement Agreement, Para. 6 and Exh. "A" thereto, Para. 6) According to Mr. Simpson, this "helps promote stability to the RARM rate while allowing the company to recover its costs if collections get too far out of sync with costs." (Exh. 3, p. 5, LL 16-17) In Year 4 and subsequent years, if the 5.25% threshold is not exceeded, the Company is required to provide a RARM True-Up calculation and additional information for the test period. (See Settlement Agreement, Para. 7 and Exh. "A" thereto, Para. 7) If the 5.25% threshold is exceeded, the Settlement Agreement allows the Company to recover the difference between the total RARM Cost actually recovered during the test period and the total RARM Cost that was last approved by the Commission, plus interest in the proposed RARM cost. (Knotts, Exh. 5, p.11, LL 17-21 & Settlement Agreement, Para. 8 and Exh. "A" thereto, Para. 8)

26. In Year 4 ending May 31, 2010 and subsequent years, if the 5.25% threshold is not exceeded in either direction for three (3) consecutive years, the threshold may be reevaluated by the parties to

determine if a more appropriate threshold should be applied. (Ex. 3, p. 6, LL 9-11 & Settlement Agreement, Para. 7)

IV. DISCUSSION & SETTLEMENT AGREEMENT

27. The Commission's authority to act in these matters derives from 26 Del. C. §§ 304 and 305 and 26 Del. C. § 1007 (c)(1)(a) of the Electric Utility Supply Act of 2006.³

28. The Settlement Agreement in this Docket is attached hereto as Exhibit "A." Its provisions are explained in Section III herein through the testimony of the Company's and Staff's witnesses. According to Delmarva's Mr. Simpson, the Settlement Agreement is in the public interest because "it allows parties to resolve the disputed issues and avoid the costs and uncertainties associated with proceeding to an evidentiary hearing." (Simpson, Exh. 3, p. 4, LL 20-21) Additionally, Mr. Simpson testified that "the settlement terms provide a balance between rate relief for the public and cost recovery for the company, while providing transparency to all parties of future RARM calculations, resulting in a settlement that benefits all parties." (Simpson, Exh. 3, p. 6, LL 17-20).

29. Mr. Simpson testified that the Settlement Agreement is in the public interest because:

- (a) "Under the terms of the Settlement, the Company will be allowed to collect the actual incremental expenses incurred in providing SOS in Year 2. Furthermore, the

³ For a brief legislative history of the Electric Supply Act of 2006 relating to RARM, see Footnote 1, *supra*.

Company has agreed to lower the carrying cost on the amount of under-collected RARM in Year 2 to 6.4% from the 10.49% allowed rate of return provided by the Commission in the Company's last base rate case. In Year 3, the allowed supply and transmission related uncollectible expense is limited to \$7,280,767 providing a cap on an expense category that has been rising significantly in recent years. In Year 4 and subsequent years, the supply and transmission related uncollectible expense component in the RARM will be the three year normalized average." (Simpson, Exh. 3, p. 5, LL 3-11)

- (b) "The parties have also agreed that the Company shall not seek approval of an increase in the RARM unless the under-collection of the proposed Total RARM Costs exceeds 5.25% of the Total RARM Cost previously approved by the Commission and will seek a decrease if the Company over-collects by more than 5.25%. This threshold helps provide stability to the RARM rate while allowing the company to recover its costs if collections get too far out of sync with costs." (Simpson, Exh. 3, p. 5 LL 12-17; Knotts, Exh. 5, p. 12, LL 17-21)
- (c) "Whether or not recovered costs are within the 5.25% threshold, the Company will continue to provide

documentation that will allow staff [and] the parties to easily review the RARM calculation without having to resort to formal discovery, saving time and expense for all parties while preserving Staff's ability to properly monitor the RARM calculations. Documentation will include:

- 1) A RARM true-up calculation;
- 2) Implementation & ongoing incremental costs;
- 3) Items identified to be recovered in supply, e.g., other taxes, 3-year rolling average of uncollectible expense, etc.;
- 4) Worksheets supporting the monthly and annual determinations of the total RARM Costs recovered and applicable monthly interest pursuant to FERC 35.19a; and
- 5) Documents the Company deems appropriate to support their determination of total RARM Cost for the Test Period."

(Simpson, Exh. 3, p. 5, LL 18-23, p.6 LL 1-8)

30. If the 5.25% threshold is not exceeded in either direction for three (3) consecutive years, the threshold may be reevaluated by the parties to determine if a more appropriate threshold should be applied. In Year 4 and subsequent years, if the 5.25% threshold is

exceeded, the Settlement allows the Company to recover the difference between the Total RARM Cost actually recovered during the test period and the Total RARM Cost that was last approved by the Commission, plus interest in the proposed RARM Cost. This provides recovery for the Company for approved costs while insulating the public from potential, large rate increases. (Simpson, Exh. 3, p. 6, LL 9-16; Knotts, Exh. 5, p. 12 LL 25-26, p. 13, LL 1-4.)

31. Without repeating Mr. Simpson's testimony described immediately above, Staff's Ms. Knotts added that the Settlement Agreement was in the public interest because:

A. The proposed Settlement Agreement is consistent with the 2005 Settlement Agreement approved in PSC Docket 04-391. (Knotts, Exh. 5, p. 12, LL 3-4; T-28) There has been the opportunity for public comment in connection with the 2005 and the proposed Settlement Agreements. (T-28)

B. In Year 4 and subsequent years, the supply and transmission uncollectible expense component in the RARM will be the prior three (3) year normalized average. (Knotts, Exh. 5, p. 12, LL 8-11; T-28) According to Ms. Knotts, this treatment is "consistent with Commission policy..." (Knotts, Exh. 5, p. 12, LL 8-11) This will also reduce administrative costs. (T-29)

C. The carrying cost for Year 4 and subsequent years applied to the under/over collections will compensate the ratepayer for the

higher cost of the individual debt (FERC 35.19a plus basis points) and compensate the Company with a fair debt rate. (See FERC *Electric Interest Rate* No. 35.19a, effective October 15, 2009). (Knotts, Exh. 5, p. 12, LL 12-16; T-29)

32. At the evidentiary hearing, the parties each testified that the settlement terms, which were reached by parties representing the interests of the Company's Delaware ratepayers and the Company's shareholders, appears to be a reasonable resolution of the issues raised by the Staff and the DPA. (T-28) Also, pursuant to 26 *Del. C.* §512, where practicable, settlements are encouraged by the Commission.

33. Michael Sheehy, Deputy Director for the Public Advocate, testified that the settlement was also in the public interest because: 1) there was adequate information and discussion between the participants for the parties to reasonably evaluate their respective positions; (T-34); and 2) Mr. Sheehy believed that the Commission would, in all likelihood, find that the settlement within a "range of reasonableness." (T-34-35)

V. RECOMMENDATIONS

34. For the reasons discussed above, I recommend that the Commission adopt as reasonable, and in the public interest, the proposed Settlement Agreement attached to the proposed Order in this matter. The Company, Staff and Delaware's Division of Public Advocate have all endorsed this settlement. Also, I recommend that the RARM factor approved by the Commission in Order 7531 (February 5, 2009) is

again approved, to be effective on or after March 2, 2009. A proposed Order, which will implement the forgoing Findings and Recommendations, is attached hereto as Exhibit "B."

Respectfully submitted,

_/s/ Mark Lawrence_____
Mark Lawrence
Hearing Examiner

DATED: December 8, 2009

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

BEFORE THE PUBLIC SERVICE COMMISSION

OF THE STATE OF DELAWARE

IN THE MATTER OF THE APPLICATION OF)
DELMARVA POWER & LIGHT COMPANY FOR)
APPROVAL TO MODIFY ITS STANDARD OFFER)
SERVICE SUPPLY RATE TO REFLECT A) PSC DOCKET NO. 09-9
REVISION TO THE REASONABLE ALLOWANCE)
FOR A RETAIL MARGIN ("RARM"), PURSUANT)
TO PSC DOCKET NO. 04-391)
(FILED JANUARY 6, 2009))

SETTLEMENT AGREEMENT

This Settlement Agreement (the "Settlement Agreement" or "Agreement"), is entered into by and among Delmarva Power & Light Company (the "Company"), the staff ("Staff") of the Delaware Public Service Commission (the "Commission") and the Division of Public Advocate ("Public Advocate" and, together with the Company and Staff, the "Parties").

WHEREAS, in PSC Order No. 6746 (Oct. 11, 2005), PSC Docket No. 04-391, the Commission approved a settlement agreement, dated July 14, 2005 (the "2005 Settlement Agreement"),¹ allowing the Company to recover, in its Standard Offer Service ("SOS") supply rate, a "reasonable allowance for retail margin" ("RARM"), which includes, *inter alia*, recovery of incremental expenses the Company incurs in providing SOS, plus an additional \$2.75 million per year, as detailed

¹ See PSC Order No. 6746, at ¶ 23. A copy of the 2005 Settlement Agreement is attached as an exhibit to the Report of the Hearing Examiner (the "HER"), dated September 1, 2005, which in turn is attached as an exhibit to PSC Order No. 6746. Capitalized terms not otherwise defined herein shall have the meanings given those terms in the 2005 Settlement Agreement, the HER and PSC Order No. 6746, as applicable.

further in the 2005 Settlement Agreement, p. 8, ¶ 4 (the "Total RARM Costs"); and

WHEREAS the 2005 Settlement Agreement required that the Company submit, "approximately four months after the start of Year 2^[2]" of the SOS procurement process, an application to revise its rates to reflect a true-up of actual Total RARM Costs incurred up to the end of Year 1. In addition, this "Year 2" application was to include a resetting of the millage rate charged to fixed price SOS customers to collect the \$2.75 million portion of the RARM based on actual collections during Year 1; and

WHEREAS, on December 27, 2007, the Company filed its first RARM application (the "Year 1" Application), in PSC Docket No. 07-364, seeking to increase the RARM established in PSC Docket No. 04-391 to reflect the actual SOS costs it incurred from May 1, 2006 to May 31, 2007. The Commission approved the Year 1 increased RARM by PSC Order No. 7406 (June 17, 2008); and

WHEREAS, on January 6, 2009, the Company filed its second RARM application, the application in the instant docket, for an increase in the RARM (the "Year 2" Application) for recovery of Total RARM Costs from June 1, 2007 through May 31, 2008, which, according to the Company, would result in an increase of \$0.32, or .2%, per month, for an average residential customer using 1,000 kWh; and

WHEREAS, on February 5, 2009, the Commission entered PSC Order No. 7531, which approved the proposed increase in the RARM for Year 2

²Under the 2005 Settlement Agreement, "Year 1", actually 13 months, is the period May 1, 2006 through May 31, 2007. "Year 2" is the period June 1, 2007 through May 31, 2008

on a temporary basis and subject to refund, with interest effective March 2, 2009 (without proration). PSC Order No. 7531 also required that notice of the proposed increase and a deadline to file objections or comments thereto be published in The News Journal and Delaware State News newspapers; and

WHEREAS Staff identified certain issues with the Year 2 Application, and, in response thereto, on July 7, 2009, the Commission entered PSC Order No. 7603, assigning the docket to Hearing Examiner Mark Lawrence for purposes of conducting an evidentiary hearing on the proposed increase in the RARM; and

WHEREAS the Hearing Examiner entered a procedural schedule, setting the matter for an evidentiary hearing on September 15, 2009; however, the hearing has been continued and is presently scheduled for November 23, 2009; and

WHEREAS, on August 4, 2009, the Parties held a workshop to discuss the issues raised by the Year 2 Application and have met on numerous occasions since that time in an effort to resolve the Year 2 Application, as well as address issues with future RARM applications; and

WHEREAS the Parties have been able to reach a consensual resolution of certain disputed issues; and

WHEREAS the notice required by PSC Order No. 7531 was published, but no comments or objections have been filed with the Commission; and

WHEREAS the Parties wish to resolve those disputed issues and avoid the costs and uncertainties associated with proceeding to an evidentiary hearing; and

WHEREAS the Parties believe that this settlement, on the terms and conditions contained herein, will serve the interests of the public and the Company, while meeting the statutory requirement that rates be both just and reasonable;

NOW, THEREFORE, IT IS HEREBY STIPULATED AND AGREED by the Parties that the Parties will submit to the Commission for its approval the following terms and conditions for resolution of the pending proceeding:

1. Except as altered by this Settlement Agreement, the 2005 Settlement Agreement is hereby incorporated herein.

2. Staff and the Public Advocate agree to recommend approval of the Year 2 Application as modified by the terms of this Settlement Agreement.

3. With respect to the Year 2 Application, the Company shall be entitled to collect, as part of its incremental expenses incurred in providing SOS, the supply and transmission-related costs of uncollectible accounts from the provision of SOS in the amount not to exceed \$6,290,039 less late payment revenues of \$2,046,385.

4. With respect to the Company's next application for an adjustment to RARM, i.e., Year 3 for recovery of Total RARM costs from June 1, 2008 through May 31, 2009, subject to the under-collection or over-collection percentages described below, the Company shall be entitled to collect, as part of its incremental expenses incurred in providing SOS, the supply and transmission-related costs of uncollectible accounts from the provision of SOS in the amount not to exceed \$7,280,767 less applicable late payment revenues.

5. Subject to the under-collection or over-collection percentages described below, in any future application beyond Year 3 for an adjustment to the RARM, the Company shall request Commission approval to include in the Total RARM Cost recovery of the supply and transmission-related costs of uncollectible accounts from the provision of SOS only by averaging such uncollectible expense over a three-year period ending May 31 of the most recent calendar year included in its application. See Exhibit A, ¶ 5.

6. With respect to any future application beyond Year 3 to adjust the RARM, the Company agrees that it shall not seek approval of an increase in the RARM unless the under-collection of the proposed Total RARM Costs exceeds 5.25% of the Total RARM Cost previously approved by the Commission. Conversely, the Company shall seek approval of a decrease in the RARM if its over-collection of the proposed Total RARM Costs exceeds 5.25% of the Total RARM Costs previously approved by the Commission. See Exhibit A, ¶ 6.

7. For any year beyond Year 3 where the Total RARM Cost does not exceed the 5.25% threshold, the Company shall provide Staff and the Public Advocate with the following for the "Test Period"³:

- a. A RARM true-up calculation;
- b. Implementation and ongoing incremental costs;
- c. Items identified to be recovered in supply, e.g., other taxes, 3-year rolling average uncollectible expense, etc.;

³ Where Test Period is the 12-month period from June 1 of the previous calendar year extending to May 31 of the most recent calendar year.

- d. Worksheets supporting the monthly and annual determinations of the Total RARM Costs recovered and applicable monthly interest pursuant to FERC 35.19a; and
- e. Documents the Company deems appropriate to support their determination of Total RARM Cost for the Test Period.

A docket shall not be required to be opened for this informational filing unless formal discovery is requested by Staff or the Public Advocate on any elements of the informational filing. In any filing regarding Total RARM Cost, the Company has the burden of supporting any element of the filing. To the extent that any element, or portion of any element, is deemed not supported, it may be challenged and subject to review by the Commission. If the Company does not exceed the threshold of 5.25% over or under collected of the Total RARM Cost for three consecutive years, the threshold may be reevaluated by the Parties in the Company's third informational filing.

8. In any future application beyond Year 3, the Parties agree that recovery of the difference between the Total RARM Cost actually recovered⁴ during the Test Period and the Total RARM Cost that was last approved by the Commission, plus interest, shall be included in the proposed Total RARM Cost. Such interest shall be calculated in accordance with the methodology set forth on Exhibit A, ¶ 8.

9. The Company, Staff and the DPA agree not to seek recovery, in any proceeding, of the difference between the rolling 3-year average of supply and transmission uncollectible expense included in the Total RARM Cost being requested and any other monthly or annual

⁴ Where the actual RARM cost recovered is determined based on the actual kWh sales by rate class and the actual RARM factor in effect

supply and transmission uncollectible expense actually incurred by the Company.

10. For purposes of settlement of this Application only, the Company shall be entitled to include a carrying cost of 6.4% on the RARM amount under-collected for Year 2 for a five-year amortization period ending February 2014. Based on the 6.4% carrying cost for Year 2 provided above and other adjustments to the proposed Total RARM Cost filed in this Application, the annual amortization amount of the Total RARM cost under-collected for Year 2 shall be \$509,122. Additionally, pursuant to Section II.G.3 of the 2005 Settlement Agreement, the Company shall be entitled to include an overall rate of return of 10.49% in the annual amortization of the Total RARM Cost under-collected for Year 1 for a five-year amortization period ending February 28, 2013. The annual amortization amount of the Total RARM Cost undercollected for Year 1 shall be \$898,233.

11. The over-recovery of the City of Wilmington franchise tax of \$609,505 shall be removed from the Application.

12. The Company will ensure that there has been no double counting of IBM invoices submitted as part of its RARM calculation in the Application by removing \$1,664 from the Application.

13. Within 10 days of execution of this Settlement Agreement, the Company shall provide to Staff and the Public Advocate a revised copy of "Attachment A" to the Application, as well as revised supporting documents, calculating an adjusted RARM on a total cost and kWh basis that conforms with the terms and conditions herein. Based

on the RARM reflecting the Year 2 adjustments to the Total RARM Costs specified above, the actual kWh billed for Year 2, i.e., June 1, 2007 through May 31, 2008, the Company shall calculate the amount of RARM cost for Year 2 actually collected from customers calculated pursuant to Exhibit A to this Settlement Agreement.

14. With respect to future applications seeking Commission approval of the adjustment to the RARM, the Company agrees that it will submit, simultaneously with the application, all supporting worksheets and other documents so that the methodologies, assumptions, and other information necessary to understand the specific relief sought by the Company. The Company further agrees that, to the extent any discovery is necessary following the filing of such applications, the Company shall fully cooperate with Staff and the Public Advocate in the timely response and/or resolution to any data requests or other discovery Staff and the Public Advocate may propound on the Company.

15. This Settlement Agreement is the product of extensive negotiation, and reflects a mutual balancing of various issues and positions. It is therefore a condition of the Settlement Agreement that it be approved by the Commission in its entirety without modification or condition. If the Settlement Agreement is not approved in its entirety, it shall become null and void, and the Application shall be re-scheduled for an evidentiary hearing before the Hearing Examiner.

16. This Settlement Agreement may be amended and/or revised to conform with Commission modifications or conditions only by the written agreement of all the Parties.

17. This Settlement Agreement may be executed in counterparts by any of the signatories hereto and transmission of an original signature by facsimile or email shall constitute valid execution of this Agreement. Copies of this Settlement Agreement executed in counterpart shall constitute one agreement. Each signatory executing this Settlement Agreement warrants and represents that he or she has been duly authorized and empowered to execute this Settlement Agreement on behalf of the respective party.

DELAWARE PUBLIC SERVICE COMMISSION
STAFF

Date:

10/30/09_____

By: /s/ Bruce H. Burcat_____

DELMARVA POWER & LIGHT COMPANY

Date:

10/29/09_____

By: /s/ Todd Goodman_____

THE DIVISION OF PUBLIC ADVOCATE

Date:

10/30/09_____

By: /s/ Michael Sheehy_____

EXHIBIT A

- ¶ 5 For example, with respect to the Company's filing of Year 4 costs, the uncollectible expense shall consist of the average of supply and transmission related uncollectible expenses for the three-year periods: June 1, 2007 to May 31, 2008 (Year 2), June 1, 2008 to May 31, 2009 (Year 3), and June 1, 2009 to May 31, 2010 (Year 4).
- ¶ 6 Year 4 - Given a Total Approved RARM cost of \$10,000,000; Threshold 5.25% = \$525,000

Over-collection example: Company actually collects \$11,000,000; exceeds threshold by \$475,000. (\$1,000,000 - 525,000 = \$475,000 above the threshold.)
For Year 5, the Company will reduce the Total Proposed RARM cost by \$1,000,000 plus the applicable interest pursuant to FERC 35.19a plus 200 basis points.

Under-collection example: Company collects \$9,000,000; below threshold by \$475,000 (\$10,000,000 - \$525,000 = \$9,475,000)
For Year 5, the Company will increase the Total Proposed RARM cost by \$1,000,000 plus the applicable interest pursuant to FERC 35.19a.

- ¶ 8 In addition to the costs provided by the Settlement Agreement approved by the Commission in Docket 04-391, the Company shall include in the proposed Total RARM Cost and kWh factor the differential, plus interest, between the previously approved Total RARM Cost and the RARM cost actually recovered during the Test Period⁵. This differential shall be calculated each month based on the following:
- o The Total RARM Cost previously approved is adjusted to reflect a monthly recovery, i.e., shall be divided by 12.
 - o The monthly RARM cost actually recovered⁶ shall be compared against the previously approved Total RARM Cost adjusted for monthly recovery to determine a monthly RARM Cost differential.
 - o Monthly interest pursuant to FERC 35.19a shall be applied to the adjusted monthly RARM Cost differential in the following manner:
 - Total monthly under-recovery shall reflect the monthly interest pursuant to FERC 35.19a.

⁵ Where Test Period is the 12-month period from June 1 of the previous calendar year extending to May 31 of the most recent calendar year

⁶ Where the actual RARM cost recovered is determined based on the actual kWh sales by rate class and the actual RARM factor in effect

- Total monthly over-recovery shall reflect the monthly interest pursuant to FERC 35.19a plus 200 basis points.
- The annual sum of the total monthly RARM cost differential amounts, plus interest, for the Test Period shall be included in the Total RARM Cost and kWh factor requested by the Company.
- For example, where the previously approved Total RARM Cost was \$12 million and the monthly recovery of RARM Cost during the Test Period was \$1 million:
 - The \$12 million would be adjusted to reflect a monthly amount, i.e., \$1 million.
 - The actual monthly RARM cost recovered would be compared to the previously approved Total RARM Cost adjusted for monthly recovery, i.e., \$1 million.
 - The differential, i.e., zero, would be reflected for that month and no interest would be applied.
- If the monthly recovery was \$900,000 then the monthly interest would be determined on the basis of an under-recovery of \$100,000 at the monthly interest pursuant to FERC 35.19a.
- If the monthly recovery were \$1,100,000 then the monthly interest would be determined on the basis of an over-recovery of \$100,000 at the monthly interest pursuant to FERC 35.19a plus 200 basis points.