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DELAWARE P.S.C.

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MEMORANDUM

TO: Robert Howatt, Executive Director

FROM: Kevin Neilson, Regulatory Policy Administrator KDN

DATE: September 23, 2013

SUBJECT: IN THE MATTER OF THE INVESTIGATION INTO DELMARVA POWER & LIGHT COMPANY'S PLANNED DISTRIBUTION INFRASTRUCTURE INVESTMENTS OVER THE NEXT FIVE YEARS (OPENED APRIL 16, 2013) – PSC DOCKET NO. 13-152

Background:

On March 22, 2013, Delmarva Power and Light Company ("Delmarva" or "Company") filed an application with the Delaware Public Service Commission ("the Commission") seeking an increase in electric base rates. The total revenue increase requested by Delmarva in this matter is $42,044,000 or 23.8% over existing retail distribution rates. In addition, Delmarva stated that it intends to invest approximately $397 million in its distribution system over the next five years to replace infrastructure and enhance and maintain system reliability (Docket No. 13-115, Direct Testimony of Michael W. Maxwell at 3, 5.) On April 16, 2013, the Staff of the Commission ("Staff") filed a motion (the Motion") requesting the Commission to open an investigation to examine Delmarva's proposed expenditures for reliability improvements over the course of the next several years to maintain adequate and reliable service. On May 7, 2013, the Commission considered the Motion and entered Order 8363 opening PSC Docket No. 13-152 for the purpose of investigating, among other things, Delmarva's proposed distribution infrastructure and reliability investments going forward for a period of up to five years, and if

such investment is consistent with Delmarva customers' reliability needs and the ability of those customers to pay for such investment.

PSC Docket 13-115

As part of its application in PSC Docket No. 13-115, Delmarva proposes to include reliability investments that it plans to make through the end of 2013 including investments that it says will enhance reliability. In its application, the Company asserts that enhanced reliability benefits its customers and is needed given the digital economy in which we live. The Company points out that improved reliability can reduce the number and duration of outages that customers experience. Delmarva also points out that better electric reliability has a positive economic impact on the State as companies locate or seek to locate in Delaware, including financial institutions that require highly reliable electric service.

The Company has included its projected 2013 reliability investments in Adjustment 26 of its filing in PSC Docket 13-115. Testimony sponsored by other participants in that docket suggests that part or all of Adjustment 26 should be rejected and excluded from the Company's rate base for rate setting purposes. The Public Advocate's Consultant's testimony suggested that "[t]he reliability investments included in this adjustment are uncertain, and from a policy perspective, not all of the investments are currently "used and useful" or entirely "known and measurable." Moreover, the investments included in Adjustment 26 are not supported by any cost-benefit or value of service studies, which should be a prerequisite for a forward-looking investment adjustment of this nature. The Company is currently exceeding the Commission's established reliability standards, which the Company advocated for and agreed to in Regulatory Docket No. 50, and thus there is no pressing need to include post-test year investments in rate base." The Public Advocate's Consultant's testimony goes on to say that "[t]he Company's past budgeting performance suggests that the budgeted investments included in Adjustment 26 may be overstated by as much as 25 percent or more. Most importantly, the omission of any defined review for appropriateness and reasonableness is a fatal flaw and should serve as a basis for summarily rejecting the Company's proposal." The Public Advocate's Consultant says that a review of the projects included in Adjustment 26 reveals that it includes "non-specific blanket projects, projects which were described as "as needed" or "as identified," projects for emergency repairs and restoration, projects associated with spares, and projects not specifically identified as being associated with any reliability improvements." In addition, Commission Staff consultants suggest that given that fact that Delmarva is already providing electric service that well exceeds the Commission approved requirement, customers should not be required to pay for infrastructure that, according to Delmarva, will enhance reliability. Staff points out that there is

no Commission, Delaware Legislative, Customer or Local Community directive to provide added reliability and therefore customers should not, necessarily, be required to pay for reliability enhancing projects merely because the Company and its shareholders have invested in them.

It does not appear that the parties are suggesting that reliability is not important, nor are they suggesting that the Company should not make investments in reliability; they are merely questioning whether customers should have to foot the bill for such reliability enhancements without some clear directive, and whether the investments that the Company is requesting are indeed related to reliability, and without public input and discussions about the need for such enhancements. The Commission has received complaints and letters in opposition of the rate increase request from customers suggesting that given the current economic situation, they cannot afford the increases that Delmarva Power is requesting. They point to the fact that most incomes are not increasing and many people are without work.

Distribution Reliability Measures

Distribution performance indicators measure the frequency and duration of customer interruptions. Interruption durations of more than five minutes are classified as sustained interruptions and those with duration of less than five minutes are classified as momentary. Most reliability indices exclude interruptions caused by major events such as adverse weather or unusual equipment failures. Some of the most commonly used indices are System Average Interruption Frequency Index ("SAIFI"), Customer Average Interruption Duration Index ("CAIDI"), System Average Interruption Duration Index ("SAIDI"), and Average Service Availability Index ("ASAI"). The Commission's regulations for electric reliability were promulgated in PSC Regulation Docket 50 and those regulations are now contained in *26 Del. Admin. C.* §3007 (the "Rules"). The SAIDI measure is a composite measure of both the average frequency and average duration indices and under the Rules, Delmarva Power is required to maintain its system such that the system wide SAIDI does not exceed (or is any worse than) 295 minutes per customer. Delmarva has continuously met and exceeded this requirement and in fact points out in its 2012 Annual Performance Report and its application in 13-115 that in 2012, its SAIDI was 146 minutes per customer; 51% lower (better) than the requirement. In accordance with the Rules, Delmarva excludes "Major Events" in the calculation of its SAIDI. "Major Event" is defined as an event consistent with the I.E.E.E.1366, Guide For Electric Power Distribution Reliability Indices standard as approved and as may change over time. Thus, the objective, and the actual performance excludes outages that occur, in many instances, during large storms. Given this fact, reliability investments that improve

SAIDI may not improve reliability or restoration times during storms. This fact, in and of itself, is not necessarily a concern, however, customers, who are being asked to pay for the investments in reliability, should to be informed of what they are being asked to pay for and what they are getting for their payment.

Delmarva's Anticipated Reliability Investment over the next 5 years

Currently a typical residential customer using 1,000 kWh receives a total bill of approximately $141.23, of which only $39.01 (less than 30%) is actually related to distribution costs. As discussed above, Delmarva has stated that it intends to invest $397 million over the next 5 years on infrastructure (2013-17). This is in addition to the revenue increase being requested in DPL's current electric base case pending before the Commission, PSC Docket 13-115. The impact of these additional investments on the distribution portion of an average residential customer's bill could be considerable. Based on Staff's best estimate and assuming no changes to other variables an average residential customer, using 1000 kWh a month, could see an increase in the distribution portion of their bill of between 25-30% over the next five years. That's an additional $9.75 to $11.70 per month, or a potential $140 more per year on the average customer's bill in 2017. This is in addition to the forecasted supply cost increases that the General Assembly has mandated as part of the 2010 Renewable Energy Portfolio Standards legislation.

In comparison, the average consumer inflation rate over the past five (5) years (as measured by the Consumer Price Index) has only been between 2.0 and 2.5%. If that rate were to continue, and Delmarva were to make all of its proposed investments, Delmarva's future rate increases would be significantly higher than the historical average inflation rate for the next five year period.

Public Discussion Forums and Public Comment Sessions

In order to better define what customers need and expect in terms of reliability, interactive discussion sessions will allow all interested parties to explore, learn, and express concerns with the current level of investment, as well as the Company's anticipated level of investment, in reliability, including how it will affect rates. In accordance with Delaware Public Service Commission Order No. 8363, the Commission Staff and Delmarva Power Company will

hold Public Interactive Discussion Forums and Comment Sessions to solicit input from the public in the Commission's investigation into

- the level of reliability that customers are currently receiving,
- the level of reliability that customers believe that they require,
- the amount of money that customers are willing to pay for that reliability,
- the affordability to customers of the current and proposed Delmarva Power rates, and
- the necessity of increasing rates, and the ability of customers to pay for those rates, that may be required if the Company makes the $397M in incremental reliability investment it has proposed over the next five years.

This is the public opportunity for Delmarva Power customers to share their views on Delmarva's proposal to increase reliability and the associated rates that may be required. The Public Interactive Discussion Forums and Comment Sessions will be held at the following times and locations:

DATE	TIME	LOCATION
Thursday, September 26, 2013	4:00 p.m.	Public Service Commission 861 Silver Lake Blvd., Suite 100 Hearing Room Dover, DE 19904
Thursday, October 3, 2013	5:30 p.m.	Delaware Tech (DTCC) Jack F. Owens Campus, Electra Hall – William Carter Partnership Center, Rt. 18 Seashore Highway, Georgetown, DE
Wednesday, October 16, 2013	7:00 p.m.	University of Delaware - Arsht Hall – 1st Floor, Rooms 108 & 109, 2600 Pennsylvania Avenue, Wilmington, DE

Upon conclusion of the public discussions and comments and the Staff review of Delmarva's planned infrastructure investment, the Staff will be reporting its findings and recommendations to the Commission for their consideration. Staff appreciates the opportunity to brief the Executive Director on this investigation and welcomes any comments that you may have.