

ORDER NO. 88567

IN THE MATTER OF THE APPLICATION OF DELMARVA POWER & LIGHT COMPANY FOR ADJUSTMENTS TO ITS RETAIL RATES FOR THE DISTRIBUTION OF ELECTRIC ENERGY <hr/>	* * * * * * * * *	BEFORE THE PUBLIC SERVICE COMMISSION OF MARYLAND <hr/> CASE NO. 9455 <hr/>
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Issue Date: February 9, 2018

I. INTRODUCTION AND EXECUTIVE SUMMARY

In this Order, we¹ approve a *Joint Motion for Approval of Agreement of Unanimous Stipulation and Settlement*² (collectively, “Settlement”). We approve the Settlement because we find that, under the circumstances and on the record before us, the unanimous agreement of the parties³ will result in just and reasonable rates for Delmarva Power & Light Company (“Delmarva” or “Company”) and its customers and is consistent with the public interest. The small rate increase contained in the Settlement, a total of \$13.4 million in distribution revenue, is significantly less than the Company’s original request of \$27,029,794, which was later revised to \$19,328,129. Although Staff has recommended an increase of \$11.1 million, and OPC has recommended an increase of \$7.2 million, we believe that the revenue increase of \$13.4 million is a reasonable compromise of all Parties’ positions and results in just and reasonable rates. We agree

¹ Commissioner Mindy L. Herman did not participate in this decision.

² *Joint Motion for Approval of Agreement of Unanimous Stipulation and Settlement* filed on December 18, 2017 (“Settlement”).

³ In addition to the Company, two other parties participated in this case: the Public Service Commission of Maryland’s (“Commission”) Technical Staff (“Staff”) and the Office of People’s Counsel (“OPC”) (collectively, with the Company, the “Parties”).

with the Parties' allocation of the base rate revenue requirement using the Two-Step method described in the Settlement and the increased customer charge.⁴

We are willing to allow the Staff to convene a work group with representatives from Delmarva and OPC to facilitate the Company's evaluation of its Maryland reliability spend plan from 2017 through 2020.⁵ The Company has agreed to report its findings to the work group 45 days prior to filing its next base rate case or by October 31, 2018, whichever is earlier, and the work group will in turn examine the Company's system average interruption frequency index ("SAIFI") and system average interruption duration index ("SAIDI") performance target through 2020 within the cost containments established in Commission Order No. 86990. The Parties have agreed that if Staff determines "that a reliability planning consulting firm is necessary to assist Staff in its evaluation, Delmarva will provide funding not to exceed \$150,000 which costs the Parties agree shall be recoverable in rates in the Company's next rate case filing."⁶ The Parties also agree that the reliability consulting firm will be selected by Delmarva and approved by Staff. We approve this element of the Settlement based on the Parties' testimony. However, the Parties' agreement is not binding on the Commission to adopt or implement any specific recommendations the work group might file, nor does it compel us to undertake further proceedings to consider them. The purpose and scope of the work group shall cover only the areas stipulated in the Settlement.

⁴ Settlement at 3.

⁵ Settlement at 4.

⁶ Settlement at 4.

II. BACKGROUND

On July 14, 2017, pursuant MD. CODE Ann., Public Utilities Article (“PUA”) §§ 4-203 and 4-204, Delmarva filed an Application with the Commission for authority to increase its retail electric rates in Maryland. The Company requested a \$27,029,794 increase in electric rates based upon a test year consisting of the 12-month period ending September 30, 2017, using seven months of actual data as of April 30, 2017 and projected data for five months ending September 30, 2017.⁷ According to the Application, the impact of the Company’s requested revenue increase would result in a 2.8 percent overall increase. Subsequently, the Company filed several rounds of testimony reflecting more accurate financial data and on November 16, 2017, Delmarva filed rebuttal testimony reflecting actual data for the 12-month period ended September 30, 2017, which resulted in the Company’s proposed increase in electric distribution rates to decrease to approximately \$19.328 million.⁸

On October 16, 2017, Staff filed direct testimony recommending that the Company be authorized to implement revised electric distribution rates that produce an increase in annual revenues of \$11.083 million.⁹ On the same day, OPC filed direct testimony recommending that the Company be authorized to increase electric distribution rates that produce an increase in annual revenues of \$5.002 million.¹⁰

⁷ Settlement Testimony of Jamie A. Smith at 1.

⁸ Settlement Testimony of Jamie A. Smith at 2.

⁹ *Id.*

¹⁰ *Id.* at 3.

III. SETTLEMENT AGREEMENT

The parties reviewed the testimony filed in this matter and unanimously determined it was appropriate to propose a settlement to the Commission in this case. On December 18, 2017, Delmarva, Staff, and OPC (collectively, the “Parties”), filed a *Joint Motion for Approval of Agreement of Unanimous Stipulation and Settlement*. The Company, Staff and OPC each filed testimony in support of the Settlement on January 2, 2018. The Commission held an evidentiary hearing on the proposed Settlement on January 5, 2018.

The Settlement provides that Delmarva shall file new base rate schedules that increase electric distribution rates by \$13.4 million.¹¹ The Settlement stipulates that the new rates will become effective as soon as reasonably practicable following issuance of the Commission’s Order approving the settlement. The Settlement stipulates that the Parties have agreed to a Two-Step allocation of base rates among all customer classes.¹² Additionally, the Parties agreed to increase the customer charge for all service classifications by 1.6 percent and the resulting charge rounded to the nearest ten cents.¹³

The Settlement stipulates that solely for the purposes of calculating the Allowance for Funds Used During Construction and regulatory asset carrying costs the cost of equity shall be 9.50 percent. The Settlement provides that in its next base rate case Delmarva will provide 12-months of actual data for its selected test year at least four weeks prior to the due date of the Parties’ direct testimony.¹⁴ The Settlement also provides that Staff will convene a work group with representatives from Delmarva and OPC to facilitate

¹¹ Settlement provision no. 2.

¹² Settlement provision no. 4.

¹³ Settlement provision no. 4.

¹⁴ Settlement provision no. 4.

Delmarva's evaluation of its Maryland reliability spend plan from 2017 through 2020. Delmarva agrees to report its findings to the work group 45 days prior to filing Delmarva's next base rate case or by October 31, 2018, whichever is earlier. The parties have agreed that if Staff determines that a reliability consulting firm is necessary to assist Staff in its evaluation, Delmarva will provide funding not to exceed \$150,000 which shall be recoverable in rates in the Company's next rate case filing. The reliability consulting firm will be selected by Delmarva and approved by Staff.¹⁵ Consistent with the Commission's determination in Order No. 88432 in Case No. 9443, the Settlement stipulates that merger synergy savings related to the Exelon – Pepco Holdings Inc. merger will be flowed through the Company's cost of service, and the Company will not be required to amortize the total projected five-year merger synergy savings evenly over five years.¹⁶ The Settlement also provides that Delmarva will be permitted full recovery of the costs the Company incurred related to RM54 implementation and requests that the Commission authorize Delmarva to use the Supplier Liability Fund to recover the Company's RM54 implementation costs. The Settlement also stipulates that Delmarva is authorized to create certain regulatory assets and liabilities related to the following: Winter Storm Stella, the Advanced Meter Infrastructure and Dynamic Pricing Programs, the Cost to Achieve Merger Synergy Savings, and the current rate case expenses for the instant proceeding.

In support of the Settlement, Delmarva submitted the testimony of Kevin M. McGowan, Vice President, Regulatory Policy & Strategy of Pepco Holdings LLC

¹⁵ Settlement provision no. 4.

¹⁶ Settlement provision no. 5.

(PHI).¹⁷ Mr. McGowan states that the Settlement is in the public interest because: (1) “the rates charged to customers are just and reasonable and recover the costs of providing safe and reliable services” to customers; (2) it balances the needs and interests of various stakeholders with adverse interests in this proceeding; and (3) it will allow all parties and the Commission to conserve resources and avoid the costs and time of conducting a full evidentiary hearing in this matter.¹⁸ Specifically, Mr. McGowan concludes that “taking into account litigation risk, cost and timing, the \$13.4 million overall revenue requirement represents a fair compromise of all Parties’ positions and results in just and reasonable rates.”¹⁹ Mr. McGowan states that the impact of the Settlement on the average residential customer using 980 kWhs per month will increase the total bill by \$2.71 or 1.9 percent. He also notes that the Company’s Class Cost of Service Study (“CCOSS”) agreed to in the Settlement will move each service classification closer to the overall unity rate of return.²⁰ Mr. McGowan testified that “due to the complexity and proprietary nature of the third-party CCOSS model software used by the Company, the Company agreed to sponsor education and training sessions for Staff and OPC to further explain how the CCOSS model functions.”²¹

Staff filed testimony of Jamie A. Smith, Director of the Commission’s Accounting Investigations Division; David Hoppock, Assistant Director of the Commission’s Electricity Division; and Kevin Zhong, Regulatory Engineer. According to Mr. Smith, Staff recommends the Settlement as a reasonable and appropriate resolution

¹⁷ PHI is the parent company of Delmarva.

¹⁸ Settlement Testimony of Kevin McGowan at 1-2.

¹⁹ *Id.* at 5.

²⁰ *Id.* at 6.

²¹ *Id.*

and notes that the “agreed upon revenue increase of \$13.4 million in annual electric distribution revenues is within a range of reasonableness.”²²

Mr. Hoppock’s testimony explains the rate design agreed upon as part of the Settlement agreement. Specifically, Mr. Hoppock notes that the Settlement allocates the revenue increase using a Two-Step method. “In Step One 6.5 percent of the total revenue increase is allocated to the under earning classes General Service Secondary Large (“LGS-S”) and General Service Primary (“GS-P”). In Step Two, the remaining revenue increase is allocated across all classes based on current distribution revenue.”²³ Mr. Hoppock testifies that the revenue allocation method in the Settlement is nearly identical to the one he originally proposed in the rate case.²⁴ Mr. Hoppock also explains that the agreed upon customer charge increase is “significantly less than Delmarva’s proposed customer charge increase of 10.5 to 34.6 percent in its initial proposal and less than the 2.84 percent increase I proposed in my direct testimony.”²⁵ Last, Mr. Hoppock testifies that the bill impact of residential customers range from 2 to 4 percent which represents a gradual increase in residential distribution bills for a wide range of residential energy consumption.²⁶

Kevin Zhong’s testimony provides analysis to support Settlement Condition 5(c) regarding the work group to be convened by Staff to facilitate Delmarva’s evaluation of its Maryland reliability spend plan from 2017 through 2020. Mr. Zhong testifies that based on the testimony and exhibits of Delmarva and its responses to Staff’s data requests provided in this case, Staff became concerned that “Delmarva Power’s reliability spend

²² Settlement Testimony of Jamie Smith at 4.

²³ Settlement Testimony of David Hoppock at 1.

²⁴ *Id.* at 1-2.

²⁵ *Id.* at 2.

²⁶ *Id.* at 3.

plan may not be cost effective in light of its reliability commitments under Order No. 86990.”²⁷ Mr. Zhong explains that Settlement Condition 5(c) provides a vehicle for Delmarva to present its reliability planning process in a transparent manner to a small work group with representatives of Staff, OPC and Delmarva. If necessary to assist the work group with its evaluation, Delmarva has agreed to provide funding not to exceed \$150,000 for a consultant to assist Staff.²⁸ The Parties agreed that the cost of the consultant is recoverable in rates in the Company’s next rate case filing. Mr. Zhong testifies that Staff performed some analysis comparing Delmarva’s reliability programs’ cost effectiveness to that of other utilities in Maryland including BGE, Choptank, Potomac Edison, Pepco and SMECO. Staff’s analysis shows that Delmarva has the highest spend per customer.²⁹ Mr. Zhong notes that “Staff concedes that reliability planning is not an exact science and that the cost effectiveness of a reliability plan is based on the types and costs of projects and programs employed by the given utility to meet its unique challenges.”³⁰ However, Mr. Zhong contends that it is not normal to expect to see such large differences in reliability cost effectiveness when compared to a sister company like Pepco.³¹ Therefore, Staff believes further investigation is warranted. Staff also believes that a better understanding should be gained in this area prior to any future rate case and in the absence of a rate case filing date Staff has set a October 31, 2018, as a reasonable deadline for completing this evaluation.³²

²⁷ Settlement testimony of Kevin Zhong at 3.

²⁸ *Id.* at 4.

²⁹ *Id.* at 6.

³⁰ *Id.* at 10.

³¹ *Id.*

³² *Id.*

OPC consultant Effron concludes that overall the Settlement terms and conditions, including the \$13.4 million revenue increase, are reasonable.³³ Mr. Effron explains the primary differences between Delmarva's revenue deficiency and OPC's position on the revenue deficiency. Specifically, Mr. Effron testifies that in its Rebuttal Testimony, Delmarva calculated a revenue deficiency of \$19.3 million whereas in his direct testimony, Mr. Effron calculated a revenue deficiency of \$5.0 million based on Dr. Woolridge's primary rate of return recommendation.³⁴ Mr. Effron further notes that the primary differences were the treatment of post-test year reliability plant additions, the use of an average vs end-of-test year rate base, the treatment of merger synergies and costs to achieve, and the proposed rates of return.³⁵ Mr. Effron agrees that accepting the revenue requirement agreed upon by the Parties is reasonable and justified and that the Settlement avoids all parties having to incur additional rate case expenses, which is beneficial to both Delmarva and its customers.³⁶

IV. COMMISSION DECISION

The Commission has considered and approved settlements proposed by adverse parties representing divergent interests in a proceeding including Delmarva.³⁷ The Commission realizes that delicate compromises are often required in order for parties to achieve an uncontested settlement. Historically, a settlement that is submitted by parties who normally have adverse interests is an indication that the overall agreement reached is

³³ Supplemental Testimony of David J. Effron at 2.

³⁴ *Id.* at 1.

³⁵ *Id.* at 2.

³⁶ *Id.* at 2-3.

³⁷ *Re Delmarva Power and Light Company*, Case No. 9249 Phase I & II, Order No. 84170, 102 MD PSC 236 (2011).

a reasonable one. However, the Commission must carefully review any settlement to ensure that the outcome is indeed reasonable. The Commission has thoroughly reviewed this Settlement and based upon the record before it the Commission approves the Settlement, as explained below.

The Parties' final revenue requirement positions ranged from a high of \$27.5 million, as proposed initially by the Company, to a low of \$5 million, advocated by OPC. Staff's final recommendation was \$11.2 million. Thus, the Settlement, with an agreed upon revenue requirement of \$13.4 million, is less than that recommended by the Company and slightly higher than what was proposed by Staff. All Parties noted that that the agreed-upon revenue requirement would render just and reasonable rates for ratepayers.

During the Settlement Hearing, the Commission questioned the need for the proposed work group in Settlement Condition 5(c) and the expectant outcome and work product of such group. Mr. Zhong provided more in-depth explanation of Settlement Condition 5(c) and why Staff believes further investigation is necessary. The Commission appreciates Staff's analysis and directs Staff to make available to the Commission a copy of the Company's reliability plan spending report that is shared with the work group.

The Commission has carefully reviewed the Settlement and finds that on the record in this case that it is in the public interest and should be approved. Specifically, the Commission finds that the \$13.4 million increase in rates, which is to be apportioned according to provision number 4 of the Settlement, will result in just and reasonable rates for all rate classes. Finally, the Commission notes and emphasizes that it shall not be

bound by any workgroup recommendations developed pursuant to this Settlement, nor to undertake further proceedings to consider them.

IT IS THEREFORE, this 9th day of February, in the year Two Thousand Eighteen by the Public Service Commission of Maryland;

ORDERED: (1) that The Application of Delmarva Power & Light Company, filed on July 14, 2017, seeking to increase electric distribution rates by \$27.03 million in its Maryland service territory is hereby denied;

(2) that the *Joint Motion for Approval of Agreement of Unanimous Stipulation and Settlement* (Settlement) is approved;

(3) that the Company shall file new tariffs that increase rates by no more than \$13.4 million, consistent with Settlement provision number 2 and 4, which shall be subject to Commission Staff verification, and Commission acceptance;

(4) that the Company is authorized to use the Supplier Liability Fund to recover the Company's RM54 implementation costs as set forth in Settlement provision 5(f);

(5) that the Company is authorized to create the regulatory assets and liabilities as set forth in Settlement provision 6;

(6) that the Company is authorized to flow through the Company's cost of service the actual synergies related to the Exelon-Pepco Holdings, Inc. merger as set forth in Settlement provision 5e; and

(7) that the Commission's Technical Staff is directed to convene a work group to facilitate the Company's evaluation of its Maryland reliability spend plan from 2017 through 2020 as set forth in Settlement provision 5(c), and to make available to the

Commission a copy of the Company's reliability plan spending report that is shared with the work group.

W. Kevin Hughes

Michael T. Richard

Anthony J. O'Donnell

Odogwu Obi Linton

Commissioners