R-00973953; R-00973953C001
C-0007
PECO Cross EX
No. 1
Phila 10/14/97
E. Hallert

September 30, 1997

Mr./Ms. L. E. G. Supplier
Licensed Electric Generation Supplier
1 Any Street
Anywhere, USA 00000

Dear Mr./Ms. Supplier:

PECO Energy Company's Power Team (Power Team) is pleased to announce an offering of products associated with the Pennsylvania Retail Access Pilot Program (Pilot) to participating Licensed Electric Generation Suppliers (LEGSs). Below is a description of our standard supply offer for load following energy and installed capacity for current PECO Energy load as well as a solicitation of market-based bids for other specific products associated with the pilot. It is our intention with this offering and solicitation to provide LEGSs with products needed to deliver reliable electricity to retail customers at competitive prices.

RETAIL PILOT STANDARD SUPPLY OFFER FOR PECO ENERGY LOAD

All-in Retail Supply

- Product Definition: the delivered product will include load-following energy and operating capacity, and installed capacity (including reserve margin obligations), and transmission and distribution losses.

- Price: the prices for this product will be equal to the customer credit in the Pilot rules for PJM energy and capacity. For residential and commercial load, this price is 3.0 cents per kWh. For industrial load, the price will be determined based on an individual customer's load characteristics. Note that, for billing purposes, the LEGSs will be responsible for remitting Pennsylvania Gross Receipts Taxes and Power Team will reduce its charge to the LEGSs accordingly.

  Power Team reserves the right to discount the above pricing prior to the close of the offering. All LEGSs will be simultaneously notified in writing of any discount that Power Team makes to all-in retail supply pricing.

- Delivery Point: retail load currently served by PECO Energy.

Amount Available

Power Team will offer each LEGS an amount of all-in retail supply equal on a capacity basis to the amount of existing PECO load won by that LEGS in the PECO Energy Retail Pilot Program.

Term

The term for purchasing all-in retail supply is for the entire duration of the Pilot, i.e. from November 1, 1997 through December 31, 1998.

Eligibility

Power Team will make these products available only to LEGSs that win existing PECO load in the PECO Energy Retail Pilot, and only in an amount equal to the LEGS's load that previously was PECO load. LEGSs must provide verification to Power Team that they have won previous PECO load in the PECO Energy Retail Pilot. (Reports required by the Pa. PUC will provide adequate verification. LEGSs must identify total loads, provide expected load profiles and a breakdown of aggregate residential and commercial versus industrial loads.)

Application

- Products: Power Team must be notified in writing of a LEGS's intention to procure the all-in retail supply product by 12:00 PM on **October 27, 1997.**

- Tariff: All LEGSs purchasing the all-in retail supply from Power Team must qualify as an Eligible Entity pursuant to PECO Energy Company's FERC Electric Tariff Volume No. 1 and must execute a Service Agreement under this tariff. Those customers who have not yet signed a Service Agreement with PECO and who wish to purchase supply from Power Team beginning on November 1, 1997, must provide Power Team with a contact from the LEGS that will facilitate the execution of a Tariff Service Agreement by **October 10, 1997**. The Service Agreement itself must be executed and delivered to Power Team by no later than **October 24, 1997**. Finally, LEGSs that purchase all-in retail supply will be required to execute a transaction letter by no later than **October 31, 1997**. Power Team will provide this letter upon notification of intention to procure all-in retail supply.

- Credit: All wholesale purchasers transacting with Power Team must comply with our Credit Policy. All credit information required to comply with the Credit Policy must be submitted to Power Team by no later than **October 10, 1997.**

For LEGSs that do not have an executed Service Agreement under PECO Energy Company's FERC Electric Tariff Volume No. 1, enclosed is a copy of the Tariff and Credit Policy.

SOLICITATION OF MARKET-BASED BIDS

In addition to the above product offerings, Power Team will accept market-based bids to procure from Power Team, individualized products for the specific purpose of supplying retail loads won within any or all of the retail pilot programs operating in Pennsylvania from November 1, 1997 to December 31, 1998. Bids should be as detailed as possible and include specific product definitions, terms, and pricing. Power Team will evaluate all bids promptly, however, notwithstanding anything contained herein to the contrary, Power Team reserves the right to reject any and all market-based bids.

GENERAL LEGS REQUIREMENT

All LEGSs wishing to purchase supply from Power Team must comply with Power Team's Tariff and Credit Policy, as set forth above. Additionally, LEGSs will be responsible for billing, collecting, reporting and remitting all applicable taxes to the approriate authorities, and shall provide to Power Team a Pennsylvania Exempt Certificate for State or Local Sales and Use Tax.

Please submit standard supply offer notifications, market-based bids, credit information, tariff information, and tax information to:

Power Team
2004 Renaissance Boulevard
King of Prussia, PA 19406
c/o Kenneth W. Cornew - PA Retail Pilot

If you have any questions, please call Ken Cornew at (610) 292-6627 or Andy Huemmler at (610) 292-6625.

For specific credit, tariff, or tax questions, please call Mike Harrington at (610) 292-6536.

Sincerely,

Nancy J. Zausner
President, Power Team

R-00973953, R-00973953
C0001 - C0007
PECO Cross Ex No 2
Phila 10/14/97
E. Hallerd

PECO Energy Restructuring Plan
Response of Delmarva Power & Light Company
to Interrogatory of Sen. Fumo
Set I - 5

Q. Please respond to the following questions which refer to the Prehearing Memorandum of the Pennsylvania Electric Competition Coalition dated September 9, 1997:

a) On page 5, please explain how the Partial Settlement produces a financial "windfall" to PECO. Is there an estimate oft he size of the "windfall?" If so, please provide a copy of that estimate accompanied by all work papers, studies, notes and other materials used in its derivation, including the name of an individual that would be available to testify on this matter.

b) On page 5, please explain how the Partial Settlement denies customers the benefits of even lower rates. Is there an estimate of the size of the rate reduction in the absence of PUC approval of the Partial Settlement? If so, please provide a copy of that estimate accompanied by all work papers, studies, notes and other materials used in its derivation. In addition, please provide the name of an individual that would be available to testify on this matter.

c) Please provide copies of any studies, documents or other materials that provide projections of the wholesale price for power that is projected for 1999 for the PJM Power Pool. In addition, please provide the name of an individual that would be able to testify on this matter.

d) What is Delmarva / Conectiv's position concerning whether or not the various charges contained in Table A of the partial Settlement include delivery charges?

e) Please provide copies of any studies or analyses that have been performed which support the statement on page 6, that the Partial Settlement fails to flow through fully to customers cost savings from planned securitization of up to $4 billion in stranded costs. In addition, please provide the name of an individual that would be able to testify on this matter.

f) Please identify any provision of the Electric Generation Customer Choice and Competition Act which may prohibit the PUC from permitting a utility to recover any increases in decommissioning costs over and above any amounts included in initial CTC recovery levels.

g) Please provide any studies that have been performed to support the statement on page 7, that the Partial Settlement could be revised to produce generation credits that are consistent with the PUC's determinations in the Pilot Order while still permitting PECO to recover its agreed upon $5.5 billion in stranded cost and still allowing the guaranteed rate decreases proposed in the settlement. In addition, please provide the name of an individual that would be available to testify on this matter.

A. See the testimony of Pennsylvania Electric Competition Coalition witnesses.

R-00973953, R-00973953 C0001-C0007
PECO Cross Exhibit No. 4
Phila 10/14/97 C. Hulburt

Docket R-00973953
PECO Interrogatory
to Delmarva Power &
Light Company

MP-1-1 Request:

a. State whether you intend to sponsor any assumptions in the current proceeding regarding future natural gas prices.

b. Identify and describe all assumptions regarding future natural gas prices that you intend to use in calculating stranded costs for PECO.

c. Set forth the factual basis for all of the assumptions identified and described in Request No. 1(b)

d. Produce all documents identified and/or described in Request No. 1(b) and (c).

e. State whether you have provided or set forth any assumptions regarding future natural gas prices in any administrative or civil proceedings since January 1, 1990, with the exception of the current proceeding. If so, please produce all documents filed and/or produced in the prior proceedings which set forth such assumptions.

MP-1-1 Response:

Delmarva has not sponsored nor does it presently intend to sponsor any witness in this proceeding regarding future natural gas prices.

DOCUMENT
FOLDER

RECEIVED
97 OCT 20 AM 9:54
PA.P.U.C.
PROTHONOTARY'S OFFICE

DOCKETED
OCT 22 1997

C:\OFFICE\WPWIN\WPDOCS\DELMARVA\RESTRUCT\INTER-MP.RSP
July 17, 1997 (1:48pm)

MP-1-2 Request:

a. State whether you intend to sponsor any assumptions in the current proceeding regarding future oil prices.

b. Identify and describe all assumptions regarding future oil prices that you intend to use in calculating stranded costs for PECO.

c. Set forth the factual basis for all of the assumptions identified and described in Request No. 2(b)

d. Produce all documents identified and/or described in Request No. 2(b) and (c).

e. State whether you have provided or set forth any assumptions regarding future oil prices in any administrative or civil proceedings since January 1, 1990, with the exception of the current proceeding. If so, please produce all documents filed and/or produced in the prior proceedings which set forth such assumptions.

MP-1-2 Response:

Delmarva has not sponsored nor does it presently intend to sponsor any witness in this proceeding regarding future oil prices.

MP-1-3 Request:

a. State whether you intend to sponsor any assumptions in the current proceeding regarding future coal prices.

b. Identify and describe all assumptions regarding future coal prices that you intend to use in calculating stranded costs for PECO.

c. Set forth the factual basis for all of the assumptions identified and described in Request No. 3(b)

d. Produce all documents identified and/or described in Request No. 3(b) and (c).

e. State whether you have provided or set forth any assumptions regarding future coal prices in any administrative or civil proceedings since January 1, 1990, with the exception of the current proceeding. If so, please produce all documents filed and/or produced in the prior proceedings which set forth such assumptions.

MP-1-3 Response:

Delmarva has not sponsored nor does it presently intend to sponsor any witness in this proceeding regarding future coal prices.

MP-1-4 Request:

a. State whether you intend to sponsor any assumptions in the current proceeding regarding future uranium prices.

b. Identify and describe all assumptions regarding future uranium prices that you intend to use in calculating stranded costs for PECO.

c. Set forth the factual basis for all of the assumptions identified and described in Request No. 4(b)

d. Produce all documents identified and/or described in Request No. 4(b) and (c).

e. State whether you have provided or set forth any assumptions regarding future uranium prices in any administrative or civil proceedings since January 1, 1990, with the exception of the current proceeding. If so, please produce all documents filed and/or produced in the prior proceedings which set forth such assumptions.

MP-1-4 Response:

Delmarva has not sponsored nor does it presently intend to sponsor any witness in this proceeding regarding future uranium prices.

MP-1-5 Request:

a. State whether you intend to sponsor any assumptions in the current proceeding regarding future O&M costs.

b. Identify and describe all assumptions regarding future O&M costs that you intend to use in calculating stranded costs for PECO.

c. Set forth the factual basis for all of the assumptions identified and described in Request No. 5(b)

d. Produce all documents identified and/or described in Request No. 5(b) and (c).

e. State whether you have provided or set forth any assumptions regarding future O&M costs in any administrative or civil proceedings since January 1, 1990, with the exception of the current proceeding. If so, please produce all documents filed and/or produced in the prior proceedings which set forth such assumptions.

MP-1-5 Response:

Delmarva has not sponsored nor does it presently intend to sponsor any witness in this proceeding regarding future O&M costs.

MP-1-6 Request:

a. State whether you intend to sponsor any assumptions in the current proceeding regarding: (1) nuclear generating plant capacity factors; and/or (2) fossil generating plant availability factors.

b. Identify and describe all assumptions regarding: (1) nuclear generating plant capacity factors; and/or (2) fossil generating plant availability factors that you intend to use in calculating stranded costs for PECO.

c. Set forth the factual basis for all of the assumptions identified and described in Request No. 6(b)

d. Produce all documents identified and/or described in Request No. 6(b) and (c).

e. State whether you have provided or set forth any assumptions regarding: (1) nuclear generating plant capacity factors; and/or (2) fossil generating plant availability factors in any administrative or civil proceedings since January 1, 1990, with the exception of the current proceeding. If so, please produce all documents filed and/or produced in the prior proceedings which set forth such assumptions.

MP-1-6 Response:

Delmarva has not sponsored nor does it presently intend to sponsor any witness in this proceeding regarding (1) nuclear generating plant capacity factors; and/or (2) fossil generating plant availability factors.

MP-1-7 Request:

a. State whether you intend to sponsor any assumptions in the current proceeding regarding: (1) load growth; and/or (2) capacity additions.

b. Identify and describe all assumptions regarding: (1) load growth; and/or (2) capacity additions that you intend to use in calculating stranded costs for PECO.

c. Set forth the factual basis for all of the assumptions identified and described in Request No. 7(b)

d. Produce all documents identified and/or described in Request No. 7(b) and (c).

e. State whether you have provided or set forth any assumptions regarding: (1) load growth; and/or (2) capacity additions in any administrative or civil proceedings since January 1, 1990, with the exception of the current proceeding. If so, please produce all documents filed and/or produced in the prior proceedings which set forth such assumptions.

MP-1-7 Response:

Delmarva has not sponsored nor does it presently intend to sponsor any witness in this proceeding regarding (1) load growth; and/or capacity additions.

MP-1-8 Request:

a. State whether you intend to sponsor any assumptions in the current proceeding regarding reserve margins and/or reserve requirements.

b. Identify and describe all assumptions regarding reserve margins and/or reserve requirements that you intend to use in calculating stranded costs for PECO.

c. Set forth the factual basis for all of the assumptions identified and described in Request No. 8(b)

d. Produce all documents identified and/or described in Request No. 8(b) and (c).

e. State whether you have provided or set forth any assumptions regarding reserve margins and/or reserve requirements in any administrative or civil proceedings since January 1, 1990, with the exception of the current proceeding. If so, please produce all documents filed and/or produced in the prior proceedings which set forth such assumptions.

MP-1-8 Response:

Delmarva has not sponsored nor does it presently intend to sponsor any witness in this proceeding regarding reserve margins and/or reserve requirements.

MP-1-9 Request:

a. State whether you intend to sponsor any assumptions in the current proceeding regarding future inflation and/or escalation factors.

b. Identify and describe all assumptions regarding future inflation and/or escalation factors that you intend to use in calculating stranded costs for PECO.

c. Set forth the factual basis for all of the assumptions identified and described in Request No. 9(b)

d. Produce all documents identified and/or described in Request No. 9(b) and (c).

e. State whether you have provided or set forth any assumptions regarding future inflation and/or escalation factors in any administrative or civil proceedings since January 1, 1990, with the exception of the current proceeding. If so, please produce all documents filed and/or produced in the prior proceedings which set forth such assumptions.

MP-1-9 Response:

Delmarva has not sponsored nor does it presently intend to sponsor any witness in this proceeding regarding future inflation and/or escalation factors.

MP-1-10 Request:

a. State whether you intend to sponsor any assumptions in the current proceeding regarding carrying the cost of capital and/or interest rates.

b. Identify and describe all assumptions regarding carrying the cost of capital and/or interest rates that you intend to use in calculating stranded costs for PECO.

c. Set forth the factual basis for all of the assumptions identified and described in Request No. 10(b)

d. Produce all documents identified and/or described in Request No. 10(b) and (c).

e. State whether you have provided or set forth any assumptions regarding carrying the cost of capital and/or interest rates in any administrative or civil proceedings since January 1, 1990, with the exception of the current proceeding. If so, please produce all documents filed and/or produced in the prior proceedings which set forth such assumptions.

MP-1-10 Response:

Delmarva has not sponsored nor does it presently intend to sponsor any witness in this proceeding regarding the cost of capital and/or interest rates.

MP-1-11 Request:

a. State whether you intend to sponsor any assumptions in the current proceeding regarding

b. Identify and describe all assumptions regarding future generating plant technology, including assumed heat rates, that you intend to use in calculating stranded costs for PECO.

c. Set forth the factual basis for all of the assumptions identified and described in Request No. 11(b)

d. Produce all documents identified and/or described in Request No. 11(b) and (c).

e. State whether you have provided or set forth any assumptions regarding future generating plant technology, including assumed heat rates, in any administrative or civil proceedings since January 1, 1990, with the exception of the current proceeding. If so, please produce all documents filed and/or produced in the prior proceedings which set forth such assumptions.

MP-1-11 Response:

Delmarva has not sponsored nor does it presently intend to sponsor any witness in this proceeding regarding future generating plant technology, including assumed heat rates.

Docket R-00973953
PECO Interrogatory
to Delmarva Power &
Light Company

MP-1-12 Request:

a. State whether you intend to sponsor any assumptions in the current proceeding regarding the cost of a new combined cycle and/or combustion turbine capacity.

b. Identify and describe all assumptions regarding the cost of a new combined cycle and/or combustion turbine capacity that you intend to use in calculating stranded costs for PECO.

c. Set forth the factual basis for all of the assumptions identified and described in Request No. 12(b)

d. Produce all documents identified and/or described in Request No. 12(b) and (c).

e. State whether you have provided or set forth any assumptions regarding the cost of a new combined cycle and/or combustion turbine capacity in any administrative or civil proceedings since January 1, 1990, with the exception of the current proceeding. If so, please produce all documents filed and/or produced in the prior proceedings which set forth such assumptions.

MP-1-12 Response:

Delmarva has not sponsored nor does it presently intend to sponsor any witness in this proceeding regarding the cost of a new combined cycle and/or combustion turbine capacity.

MP-1-13 Request:

a. State whether you intend to sponsor any assumptions in the current proceeding regarding transmission constraints.

b. Identify and describe all assumptions regarding transmission constraints that you intend to use in calculating stranded costs for PECO.

c. Set forth the factual basis for all of the assumptions identified and described in Request No.13(b)

d. Produce all documents identified and/or described in Request No. 13(b) and (c).

e. State whether you have provided or set forth any assumptions regarding transmission constraints in any administrative or civil proceedings since January 1, 1990, with the exception of the current proceeding. If so, please produce all documents filed and/or produced in the prior proceedings which set forth such assumptions.

MP-1-13 Response:

Delmarva has not sponsored nor does it presently intend to sponsor any witness in this proceeding regarding transmission constraints.

MP-1-14 Request:

a. State whether you intend to sponsor any assumptions in the current proceeding regarding the possible extension of existing generating plant facilities.

b. Identify and describe all assumptions regarding the possible extension of existing generating plant facilities that you intend to use in calculating stranded costs for PECO.

c. Set forth the factual basis for all of the assumptions identified and described in Request No. 14(b)

d. Produce all documents identified and/or described in Request No. 14(b) and (c).

e. State whether you have provided or set forth any assumptions regarding the possible extension of existing generating plant facilities in any administrative or civil proceedings since January 1, 1990, with the exception of the current proceeding. If so, please produce all documents filed and/or produced in the prior proceedings which set forth such assumptions.

MP-1-14 Response:

Delmarva has not sponsored nor does it presently intend to sponsor any witness in this proceeding regarding the possible extension of existing generating plant facilities.

MP-1-15 Request:

a. State whether you intend to sponsor any assumptions in the current proceeding regarding the cost of sulfur dioxide (SO_2) emissions.

b. Identify and describe all assumptions regarding the cost of sulfur dioxide (SO_2) emissions that you intend to use in calculating stranded costs for PECO.

c. Set forth the factual basis for all of the assumptions identified and described in Request No. 15(b)

d. Produce all documents identified and/or described in Request No. 15(b) and (c).

e. State whether you have provided or set forth any assumptions regarding the cost of sulfur dioxide (SO_2) emissions in any administrative or civil proceedings since January 1, 1990, with the exception of the current proceeding. If so, please produce all documents filed and/or produced in the prior proceedings which set forth such assumptions.

MP-1-15 Response:

Delmarva has not sponsored nor does it presently intend to sponsor any witness in this proceeding regarding the cost of sulfur dioxide (SO_2) emissions.

MP-1-16 Request:

a. State whether you intend to sponsor any assumptions in the current proceeding regarding the cost of nitrogen oxides (NO_x) emissions.

b. Identify and describe all assumptions regarding the cost of nitrogen oxides emissions that you intend to use in calculating stranded costs for PECO.

c. Set forth the factual basis for all of the assumptions identified and described in Request No. 16(b)

d. Produce all documents identified and/or described in Request No. 16(b) and (c).

e. State whether you have provided or set forth any assumptions regarding the cost of nitrogen oxides emissions in any administrative or civil proceedings since January 1, 1990, with the exception of the current proceeding. If so, please produce all documents filed and/or produced in the prior proceedings which set forth such assumptions.

MP-1-16 Response:

Delmarva has not sponsored nor does it presently intend to sponsor any witness in this proceeding regarding the cost of nitrogen oxides (NO_x) emissions.

MP-1-17 Request:

a. State whether you intend to sponsor any assumptions in the current proceeding regarding availability and/or transmission of energy and capacity from other power pools and/or reliability councils to the PJM.

b. Identify and describe all assumptions regarding availability and/or transmission of energy and capacity from other power pools and/or reliability councils to the PJM that you intend to use in calculating stranded costs for PECO.

c. Set forth the factual basis for all of the assumptions identified and described in Request No. 17(b)

d. Produce all documents identified and/or described in Request No. 17(b) and (c).

e. State whether you have provided or set forth any assumptions regarding availability and/or transmission of energy and capacity from other power pools and/or reliability councils to the PJM in any administrative or civil proceedings since January 1, 1990, with the exception of the current proceeding. If so, please produce all documents filed and/or produced in the prior proceedings which set forth such assumptions.

MP-1-17 Response:

Delmarva has not sponsored nor does it presently intend to sponsor any witness in this proceeding regarding availability and/or transmission of energy and capacity from other power pools and/or reliability councils to the PJM.

MP-1-18 Request:

a. State whether you intend to sponsor any assumptions in the current proceeding regarding availability and/or transmission of energy and capacity from the PJM to other power pools and/or reliability councils.

b. Identify and describe all assumptions regarding availability and/or transmission of energy and capacity from the PJM to other power pools and/or reliability councils that you intend to use in calculating stranded costs for PECO.

c. Set forth the factual basis for all of the assumptions identified and described in Request No. 18(b)

d. Produce all documents identified and/or described in Request No. 18(b) and (c).

e. State whether you have provided or set forth any assumptions regarding availability and/or transmission of energy and capacity from the PJM to other power pools and/or reliability councils in any administrative or civil proceedings since January 1, 1990, with the exception of the current proceeding. If so, please produce all documents filed and/or produced in the prior proceedings which set forth such assumptions.

MP-1-18 Response:

Delmarva has not sponsored nor does it presently intend to sponsor any witness in this proceeding regarding availability and/or transmission of energy and capacity from the PJM to other power pools and/or reliability councils.

MP-1-19 Request:

a. State whether you intend to sponsor any assumptions in the current proceeding to forecast: (1) annual electricity production; and/or (2) the annual market electricity price.

b. Identify and describe the analytical model that you intend to use to forecast: (1) annual electricity production; and (2) the annual market electricity price in calculating stranded costs for PECO.

c. Set forth the basis for your choice of the model identified and described in Request No. 19(b)

d. Produce all documents identified and/or described in Request No. 19(b) and (c).

e. State whether you have provided or set forth any analytical model used to forecast: (1) annual electricity production; and/or (2) the annual market electricity price in any administrative or civil proceedings since January 1, 1990, with the exception of the current proceeding. If so, please produce all documents filed and/or produced in the prior proceedings which set forth such analytical model.

MP-1-19 Response:

Delmarva has not sponsored nor does it presently intend to sponsor any witness in this proceeding to forecast: (1) annual electricity production; and/or (2) the annual market electricity price.

MP-1-20 Request:

a. State whether you intend to forecast in the current proceeding the annual electricity production and/or the annual market electricity price.

b. Identify and describe the time periods for which you intend to forecast annual electricity production and/or the annual market electricity price in calculating stranded costs for PECO.

c. Set forth the basis for your choice of the time periods identified and described in Request No. 20(b)

d. Produce all documents identified and/or described in Request No. 20(b) and (c).

e. State whether you have provided or set forth any forecasts of annual electricity production and/or the annual market price in any administrative or civil proceedings since January 1, 1990, with the exception of the current proceeding. If so, please produce all documents filed and/or produced in the prior proceedings which set forth such assumptions.

MP-1-20 Response:

Delmarva has not sponsored nor does it presently intend to sponsor any witness in this proceeding to forecast the annual electricity production and/or the annual market electricity price.

MP-1-21 Request:

a. State whether you intend to model any NERC region/subregion in the current proceeding.

b. Identify and describe each NERC region/subregion that you intend to model in calculating stranded costs for PECO.

c. Set forth the basis for your choice of the power pools identified and described in Request No. 21(b)

d. Produce all documents identified and/or described in Request No. 21(b) and (c).

e. State whether you have attempted to model any NERC region/subregion in any administrative or civil proceedings since January 1, 1990, with the exception of the current proceeding. If so, please produce all documents filed and/or produced in the prior proceedings which set forth such models.

MP-1-21 Response:

Delmarva has not sponsored nor does it presently intend to sponsor any witness in this proceeding to model any NERC region/subregion in the current proceeding.

MP-1-22 Request:

a. State whether you intend to adopt and/or sponsor in the current proceedings any projected energy prices to derive the revenue of each generating unit in calculating the respective unit's stranded costs.

b. Identify and describe the projected energy prices that you propose to use to derive each generating unit's revenue in calculating the respective unit's stranded costs for PECO.

c. Set forth the basis for the projected energy prices identified and described in Request No. 22(b)

d. Produce all documents identified and/or described in Request No. 22(b) and (c).

e. State whether you have adopted and/or sponsored any projected energy prices used to derive the revenue of each generating unit in calculating the respective unit's stranded costs in any administrative or civil proceedings since January 1, 1990, with the exception of the current proceeding. If so, please produce all documents filed and/or produced in the prior proceedings which set forth such projected energy prices.

MP-1-22 Response:

Delmarva has not sponsored nor does it presently intend to sponsor any witness in this proceeding to project energy prices to derive the revenue of each generating unit in calculating the respective unit's stranded costs.

R-00973953; R-00973953 C0001 - C0007

PECO Cross Exhibit No. 35
~~Photo 10/14/97~~
C. Nelson

Delmarva Power

eter F. Clark
Assistant General Counsel

800 King Street • P.O. Box :
Wilmington, DE 19ᴇ
(302) 429-3ᴄ
Fax: (302) 429-3ᴇ

September 12, 1997

97 OCT 20 AM 9:55
PROTHONOTARY'S OFFICE

HAND DELIVERY

Mr. Bruce H. Burcat
Executive Director
Delaware Public Service Commission
1560 S. DuPont Highway
Dover, DE 19901

RE: PSC Docket 97-229

Dear Mr. Burcat:

Enclosed are an original and 10 copies of Delmarva's comments on Staff's report on electric industry restructuring. Copies have been provided to the Commissioners as well as to all members of the service list in this docket.

Please contact Bill Moore at 302-429-3630 or me if you have any questions or concerns about the enclosed comments.

Very truly yours,

Peter F. Clark /ap

Peter F. Clark

PFC/mar
Enclosures
cc: The Honorable Robert J. McMahon
The Honorable Joshua M. Twilley
The Honorable John R. McClelland
The Honorable Arnetta McRae
The Honorable Donald J. Puglisi
Service List

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OCT 22 1997

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PSC DOCKET NO. 97-[1]
September 4, 1997

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---

[1] Same as Docket No. 96-83 with the addition of Gary R. Alexander.

John F. Dudley, Esq.
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Restructuring The Electric Industry In Delaware

Delmarva Power & Light Company's Comments on the Report by The Delaware Public Service Commission Staff

PSC Docket No. 97-229

September 12, 1997

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INTRODUCTION

Delmarva & Light Company ("Delmarva" or the "Company") supports electric industry restructuring. The Company believes that, done properly, restructuring will benefit residential consumers, businesses, and the overall economic well-being of the State of Delaware by allowing choice among retail electricity suppliers and improving the way in which monopoly electricity distribution services are priced. Delayed implementation of electricity supplier choice is not a viable option and may disadvantage Delaware.

Putting Restructuring in Perspective

Electric industry restructuring involves giving customers the opportunity to choose their electricity suppliers. (Restructuring is commonly referred to as retail access, open access, customer choice and/or restructuring.) This allows the price and terms and conditions under which electricity is supplied to customers to be determined by market forces, instead of by a regulatory agency's determination of the embedded, book cost of providing electric service. In Delmarva's view, restructuring also should involve the improved regulation of the electricity distribution function, which will remain a natural monopoly after customers are able to choose their electricity supplier. The objectives of this improvement in regulation should be to reduce distribution the cost of regulation itself and to give utilities financial incentives to reduce costs and improve service.

Electric industry restructuring necessarily involves dismantling a well-established regulatory regime. The most significant aspect of this change is the elimination of an incumbent utility's valuable franchise right to be the exclusive supplier of electricity to customers in a defined service territory. While, as noted, the electricity distribution function will remain a monopoly, the utility's monopoly on supplying electricity will no longer exist, because the utility and others will compete to supply electricity to customers in what was formerly an exclusive service territory. In other words, except perhaps as a supplier of last resort and then at a market price, incumbent utilities will no longer have the right or obligation to supply electricity to existing and new customers in a defined service territory.

Key Elements of Successful Electric Industry Restructuring in Delaware.

It is critical to the success of electric industry restructuring in the State of Delaware that incumbent utilities be permitted to compete fairly with other electricity suppliers from the onset of deregulation.

While these comments contain numerous detailed responses to Staff's report, there are three changes that must be made to Staff's proposal to create an effective, workable customer choice plan. The three changes are discussed below:

1. The incumbent utility's generating assets must be deregulated at the start of the transition to a competitive electricity supply market.

A transition to competition among electricity suppliers that continues the incumbent utility's obligation to serve at a capped regulated or "standard offer" price will necessarily retard the formation of a truly competitive electricity supply market by withholding the incumbent utility's generating assets from that market. It is likely, moreover, that the creation of such a two-tiered pricing regime will distort the market for electricity. The existence of a two-tiered pricing regime allows customers who have attractive usage characteristics -- and thus a below-average cost of service -- to opt for market-priced electricity. Since higher-than-average cost customers would likely pay higher-than-current-tariff prices in the market, under Staff's proposal, the incumbent utility will be obliged to continue to serve them at a capped regulated or standard offer rate. By definition, those customers will be no worse off than they would have been had price regulation continued, as Staff contends is necessary, only if the regulated or standard offer rate they pay is subsidized in some fashion, or if the utility is not given the opportunity to earn a fair return on its investment.

The simpler and better solution is to deregulate the generating assets of all incumbent utilities immediately and to make the incumbent utility the supplier of last resort at a market-based price plus an appropriate administrative cost charge.

2. As compensation for the incumbent utility's loss of its valuable franchise right to supply electricity to customers in a defined service territory, full "stranded cost" recovery must be allowed.

Stranded costs include the net value of (i) above-market generating assets installed or purchases made to satisfy the utility's legal obligation to serve and (ii) regulatory assets accrued under the existing regulatory regime.[1] In Delmarva's case, recovery of net stranded costs is manageable and should be accomplished for the most part by using a modest, non-bypassable Market Transition Charge (the "MTC") except for nuclear decommissioning costs, which are mandated and subject to change. The MTC should be collected over a fixed, four-year recovery period beginning in 1999. Delmarva differs from Staff on this issue. Delmarva believes that the MTC should be an access-type charge, not a per kWh charge as advocated by Staff. The MTC should not be subject to a "true-up" at the end of the transition period.

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[1] Delmarva is particularly troubled by Staff's singling out of the Company's PECO Energy power purchase. A disallowance of the costs of that purchase may be ordered, of course, only after affording Delmarva procedural due process, as mandated by Delaware law, and showing that the purchase, when made, involved waste, bad faith, or an abuse of discretion. More fundamentally, the PECO Energy purchase was a way in which Delmarva satisfied its legal obligation to serve customers in the former Conowingo Power Company service territory and the rest of its franchised service area. The Company cannot fairly be faulted for meeting its legal obligation to serve by contracting for a reliable supply of market-priced electricity.

3. Performance-based ratemaking ("PBR") principles should be used to set the price charged for delivering electricity to Delaware's homes and businesses.

There is no reason to delay implementing this improvement in the way in which monopoly distribution services are priced and thus achieving the reduced regulatory expense and efficiency improvements promised by a well-designed PBR regime. The distribution component of the electric business cannot benefit from competition and deregulation, but traditional regulation can be improved upon with a PBR that incents good performance and controls prices in a way that more closely mimics a competitive market. The concerns about PBR raised in the Staff report can be addressed through proper PBR design.

Delmarva's "Strawman" Restructuring Proposal.

In late 1996, Delmarva developed and presented its own proposed framework, or "strawman", for restructuring, as part of the Delaware Collaborative for Retail Competition. Key elements of the strawman included:

- A four-year phase-in to choice, beginning with 10% of customers on January 1, 1999[2]; 20% on January 1, 2000; 40% on January 1, 2001; 70% on January 1, 2002; and 100% on January 1, 2003.
  - The same percentage of each customer class, in terms of energy/load, to be opened to competition at same time.
  - Customer selection to be determined by lottery. Customers must elect 100% of load by location.
  - For customers who did not/could not choose, Delmarva to continue to provide energy, at least through the transition period.
- Rates to be unbundled beginning January 1, 1999.
- During the transition period, a generation price subdivided into 2 components: a retail market energy supply price (based on an estimate of market prices for 1999-2002) and a MTC to recover stranded costs.

[2] Staff recommends beginning in April 1999 and Delmarva does not object to that start date.

- Elimination of the fuel adjustment clause as of December 31, 1998. Any remaining deferred fuel balance to be recovered or credited via a "correction factor" in 1999.

- For customers who do not yet have the option to choose another supplier, the total generation price (energy supply plus MTC) to be fixed at 1998 levels for 1999 through 2002. Prices for generation to be determined by the market beginning January 1, 2003.

- Continued regulation of the distribution delivery charge under PBR plan beginning January 1, 1999, subject to periodic Commission review.

- Stranded costs will be recovered from all customers via a non-bypassable MTC charge from 1999-2002 (with the exception of nuclear decommissioning costs, which will be recovered over the plants' remaining lives).

Delmarva believes that its proposals present a useful framework for transitioning to competition in the electric industry.

Two Cautionary Notes

The General Assembly has sought the Commission's views on electric industry restructuring. The procedure adopted in this docket creates multiple opportunities for comment.

That procedure does not create, however, a means for resolving disputed issues of fact or law. Accordingly, unless there is consensus, the Commission should be cautious in endorsing any particular approach to industry restructuring, particularly if the resolution of disputed factual or legal issues might influence the Commission's view on the merits of a proposed restructuring paradigm.

Delmarva also believes that a thorough review of the Public Utilities Act of 1974 and the State's utility-related taxes should be undertaken as part of electric industry restructuring in Delaware. The need for statutory change will depend, of course, on exactly how electric industry restructuring is accomplished.

This introduction focuses on Delmarva's main points raised by Staff's recommendations for electric industry restructuring. The remainder of Delmarva's comments follow the sections of

Staff's Report, restating Staff's position where appropriate and then discussing Delmarva's position on major issues. Not commenting on a specific point does not necessarily mean that Delmarva agrees or disagrees with Staff's views.

1.0 Staff's Introduction and Background

1.1 Background

No comment.

1.2 Current Electricity Market in Delaware

No comment.

1.3 Application of Restructuring Policies to the Cooperative and Municipal Utilities

STAFF'S POSITION

Staff believes that the Delaware Electric Cooperative ("DEC") and the municipal utilities may require different treatment and policies from an investor-owned utility. Staff notes the difference in size, financial risk and tax treatments. Staff recommends that the Commission impose a reciprocity obligation for municipals (Section 3.5) and seeks comments on this issue.

DELMARVA'S POSITION

Delmarva believes that all electric customers should be provided with comparable choices and all electric markets should be opened to competition. As noted in the Staff Report, the Commission does not currently have the authority to require municipal utilities to provide their customers with retail access. In this regard, Staff recommends that the Commission impose a reciprocity obligation whereby any municipal utility wishing to sell retail supply services in any other service territory must first allow retail access to its own customers.

Delmarva agrees with Staff's reciprocity proposal. Until such time as the municipal utilities provide retail access for their own customers, Delmarva requests that the Commission exclude municipals from offering electric supply services to customers of Delmarva and DEC. Delmarva further requests that the implementation policies for retail access apply equally to Delmarva and DEC.

1.4 Structure of Staff's Report

No comment.

2.0 Overall Goals and Principles of Restructuring

STAFF'S POSITION

Staff acknowledges that there is no guarantee that industry restructuring will benefit all customers equally, or that rates will be substantially reduced. Staff recommends that competition should be implemented in a manner that ensures that all customers are no worse off than under the present system. Staff then recommends nine principles to govern restructuring as follows:

1. All electric services should remain subject to some form of regulatory oversight until there is a demonstration that the market for those services is workably competitive.

2. Where the conditions for competitive electric service markets do or could exist, competition should be allowed to emerge and flourish.

3. Conditions that foster fair competition among all suppliers must be put in place, and barriers that hinder fair competition among all suppliers must be removed, to the extent possible.

4. All customers must have an equal opportunity to participate in, and benefit from, competitive electric service markets.

5. All customer classes must be granted access to competitive electricity markets at the same rate and in the same proportion.

6. Public policy goals related to equity, availability, affordability, safety and reliability, supply-side and demand-side efficiency, environmental protection, resource diversity, and economic development must be maintained or enhanced.

7. All customers must continue to share in the costs of policies and mechanisms that benefit the public interest.

8. Utilities should be provided with the opportunity, but not the guarantee, to recover a fair share of non-mitigable, prudently-incurred stranded generation costs.

9. All stakeholders should have an opportunity to participate in the creation of policies, regulations, and legislation that guide Delaware's restructuring activities.

DELMARVA'S POSITION

Fundamental to any principles adopted by the Commission are the concepts of symmetry and fairness, and the ability of regulators to focus on making major policy decisions in a timely manner, thereby avoiding over-analysis and lengthy litigation of minor issues. To the extent possible, the competitive market should be left to determine the most efficient methods of resolving restructuring issues. As demonstrated in other industries which have transitioned from regulated to unregulated markets, regulators would play a more beneficial role if they focused on the removal of obstacles to competition for consumers, rather than by over-managing the transition, or re-regulating generating supply.

Delmarva's views of key principles are set forth in the Introduction and can be summarized as follows:

- Fair competition for all participants;
- The Commission should support the development of a vibrant competitive generation market;
- Full recovery of stranded costs, and
- Performance-based ratemaking for the monopoly distribution business.

Delmarva offers the following comments on Staff's nine principles:

- Delmarva disagrees with Principle 1. The generation business should be deregulated at the beginning of retail access. The adoption of this principle does not support the development of a vibrant competitive market.
- Adoption of Principles 2-5 are appropriate and are consistent with Delmarva's key principles. However, Principle 5 may not be administratively workable in the first year or two of the transition period.
- Delmarva does not support the adoption of Principle 6. Adoption of this principle may create barriers to the development of a vibrant competitive market and undue sound decisions already made by the Commission on some of the items listed by Staff.

- Adoption of Principle 7 is appropriate.

- Delmarva does not support the adoption of Principle 8 if the intent is to inappropriately restrict the recovery of stranded costs.

- Principle 9 is appropriate.

One of the main themes of the Staff's report is that no customer should be made worse off as a result of restructuring. Delmarva believes that following this approval could seriously undermine the achievement of the benefits available in a competitive generation market. Because of differences in the cost of serving customers (due to such factors as time-of-use, size, and load factor) and cross-subsidies inherent in the current average cost-based class rates, it is neither efficient nor desirable to guarantee that all customers will be better off under retail access. Pursuing this objective will greatly reduce the potential benefits of retail access, and could undermine the financial viability of incumbent utilities.

For economic efficiency, customers should pay the market price of the service they receive. Attempting to ensure that high cost customers are no worse off under retail access will mean that they pay less than the appropriate market price (marginal cost of the last unit dispatched). Charging customers a price that is less than marginal cost will cause them to over-consume and will prevent resources from being allocated to their highest valued use. Setting rates below market levels and below marginal cost will also result in the utility not being willing to make investments to provide safe and reliable service and to meet load growth.

In addition, attempting to ensure that no customer is made worse off will lead to the formation of a two-tiered price system in which customers that benefit from obtaining electric supply services from the competitive market (generally customers whose cost to serve is low) will take the market option, whereas customers that benefit from purchasing their electric supply on the regulated tariff (generally customers whose cost to serve is high) will pursue the regulated option. The ultimate result is that the utility will be left with customers that are, on average, more costly to serve.

3.0 Customer Choice

3.1 Increasing Pressures to Provide Customer Choice of Retail Generation Services

No comment.

3.2 & 3.3 Implications/Potential Benefits and Costs of Introducing Retail Choice

<u>STAFF'S POSITION</u>

Staff believes that there are benefits and costs associated with customer choice. Staff believes the principal benefits are:

- Competition will lower future costs;
- Risk shifts from ratepayers to generation company; and
- Competition will drive innovation of new products and services.

Staff believes the principal costs are:

- In a competitive market, it is more difficult to ensure safe, reliable, low-cost service;
- Many consumers may not have meaningful access to competition because of information requirements or buying power;
- Commission will lose jurisdiction over generation pricing and planning, thereby reducing its options for establishing generation policies that serve the public interest;
- High-cost regions may be better off under retail competition, and currently low-cost regions may be worse off; and
- In addition, in low-cost regions, utilities with generating plants whose embedded costs are below market value may be able to increase their generation prices to the market level.

<u>DELMARVA'S POSITION</u>

Delmarva believes that there will be substantial benefits that far outweigh the costs associated with electric industry restructuring.

Benefits

Restructuring is expected to result in the following benefits.

1. Increased efficiency (in the economic literature this is referred to as technical efficiency). The increase in efficiency will result in lower costs to all customers. The efficiency benefits of competitive markets are described by Alfred Kahn, a noted economist and head of the Civil Aeronautics Board during the deregulation of the airline industry.[3]

   The removal of regulatory restrictions and the pressures of competition have yielded marked increases in productivity. The failure of the airline industry to realize the huge potential economies of hub and spoke operations under regulation testifies eloquently to the inefficiency of centralized government planning and the superiority of unconstrained profit-seeking in free markets Similarly, the freedom of both airlines and truckers to vary their effective charges from one moment and one route to another, depending on the relationship between demand and capacity, has contributed powerfully to improved use of equipment and consequent reductions in cost.

   All this has occurred with no evident sacrifice of safety. With the glaring exception of the general decline in the quality of the air travel experience, it has on the whole resulted in improved quality as well as variety of service, just as any student of competition would have predicted.

[3] Alfred E. Kahn and William E. Taylor, *The Pricing of Inputs Sold to Competitors: A Comment*, 11 YALE J. ON REG. 225-40 (1994).

2. The introduction of new products and services designed to better meet customer needs.

3. Increased efficiency and customer welfare resulting from customers being charged the marginal cost of providing the services they desire. Charging customers the marginal cost of producing the services will ensure that they consume the correct quantity of electricity and that resources are allocated to their highest valued uses.

4. The risks of future generation investments will be borne by the companies making the investments, not by electric customers.

5. The cost of regulation is expected to be substantially reduced.

Costs

There will also be costs as a result of restructuring, although these are likely to be considerably less than the benefits. These costs include:

1. The process of choosing among multiple choices of vendors and products, as well as greater complexity in metering and billing. Dealing intelligently with these will require a considerable amount of consumer education. However, by offering customers both unbundled and rebundled services, it will be possible to provide customers with products that are more tailored to their needs and reduce the complexity associated with multiple options.

2. Greater volatility in the market price of electricity than under traditional regulation. However, this can be dealt with through the use of hedging techniques, such as contracts for differences.[4]

[4] Contracts for differences are agreements in which one party (usually a generator) agrees to pay the other party (usually a customer) the difference between the spot price and a strike price if the

3. In addition, some customers, who are now paying less than the cost of service, will pay more; while others paying rates higher than their cost of service will pay less. However, as competition increases efficiency and the general level of industry costs fall, it is likely that, over time, all customers will benefit.

4. Retail access is expected to require substantial costs, both to design and to implement the systems, and to install the equipment required to implement customer choice. It is also expected that substantial resources will be required to provide the information and training required for customers to realize the full benefits of restructuring.

It is crucial that sufficient time, attention, and resources be given to the resolution of the technical and logistical problems associated with customer choice.

Taxes

Besides the issues discussed above, Delmarva believes that the General Assembly and Commission should also consider the impact of restructuring on taxes.

Under Delaware's current tax structure, the deregulation of the sale of electricity may give an unfair pricing advantage to out-of-state suppliers. Under current law, the Delaware public utilities "is imposed upon any distributor of public utilities, which tax shall be at 4.25% of the gross receipts or tariff charges received for such commodities and services distributed within this state." §5502(b)(1). A distributor is defined as

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spot price exceeds the strike price. The reverse occurs if the spot price is less than the strike price. The arrangement results in the customer always paying an effective price equal to the strike price.

"any company, corporation, person or group of persons which supplies any public utility for sale to ultimate consumers or users within this State."

The General Assembly has recently enacted changes to the tax law to "level the playing field" and eliminate the unfair pricing advantage with respect to sales of gas (House Bill 320). The intent of this legislation is to subject all sales of natural gas to the public utility tax. The new law imposes the public utility tax directly on the consumer when gas is delivered in this State by a transmission company from a person who does not report and remit the tax on such gas. Taking a similar approach to taxing electricity usage would help preserve state tax revenues.

Delaware law also imposes a 0.1% tax on the value of electricity generated in Delaware. This tax provision puts Delaware electric generators at a competitive disadvantage, since out-of-state suppliers are not subject to this tax. While most of the surrounding states have gross receipts or sales taxes that are similar to the public utility tax, few states impose a tax on the value of electric generation. In a deregulated environment, a tax on electricity generated in the State of Delaware will hinder the competitiveness of Delaware's electricity.

In addition to ensuring that all sellers or consumers are subject to the public utilities tax, Delmarva proposes that any taxes on electricity should be based on kilowatt hours sold instead of gross receipts. This tax structure eliminates the problem of decreased tax revenue due to decreased electric prices. Sufficient nexus with the state for purposes of taxation can be bolstered by requiring that other suppliers, brokers and marketers obtain a license in order to sell electricity in Delaware. A condition of the license should be that the supplier, broker or marketer agrees to collect and remit the tax to the Delaware Division of Revenue.

3.4 Schedule and Process for Introducing Customer Choice in Delaware

STAFF'S POSITION

Staff recommends that retail access be phased in over four years from April 1, 1999, through April 1, 2003, in increments equal to 25% of load, with retail access to be allowed at the same rate and in the same proportion for each class. The selection process for residential and small commercial customers eligibility would be determined through a lottery and limited to 25% of customers. All large commercial and industrial customers will be allowed to participate in open access; however, each large customer would be limited to purchasing a portion of its load in each hour based on the allotted portion in that year.

DELMARVA'S POSITION

While Delmarva's "strawman" discussed earlier recommends a four-year phase in beginning in January, 1999, Delmarva can support Staff's proposal of retail access consisting of a four year phase-in approach in increments of 25% of Delmarva's load per rate class from April 1, 1999 through April 1, 2003. However, for logistical reasons, it would be preferable to start with a lower percentage of customers (perhaps 10%) in the first year, escalating in each successive year. Delmarva also believes that there may be implementation issues with Staff's proposed selection process with the use of a lottery where some randomly selected residential and small commercial customers have open access for their total load, while allowing all large commercial and industrial customers to allocate only a pro-rata share of their total load per phase-in year to their alternative energy supplier(s). In addition, Delmarva believes that having the approximate 700 large commercial and industrial Delaware customers only allowed to allocate a pro-rata share of their total load per phase-in year to their alternative energy supplier(s), can cause Delmarva's fuel costs and capacity requirements to be proportionally higher, since the alternative energy suppliers or aggregators are likely to contract for the customer's base load at 100% load factor, leaving Delmarva with the requirement and obligation to serve and supply all of the customer's more costly variable load. Further, Staff's proposal, which requires partial requirement contracts for each of the 700 large commercial and industrial customers, will also encourage the use of multiple energy suppliers. This will increase the complexity and administrative cost to Delmarva and to each alternative energy supplier for the daily administration of the scheduling, balancing, reconciling and settling of each customer's partial requirement contract(s) with each of their energy supplier during the phase-in period and beyond. Finally, Delmarva, after executing a confidentiality agreement, will need a current copy of each customer's partial requirement contract(s) with their alternative energy supplier(s) to interpret the te... of such contracts in order to perform the daily administration associated with the scheduling, reconciling and settling of energy delivered.

Regardless if Staff's phase-in at 25% of load approach, or if the Company's preferred approach is used for the selection process and the amount of customer's load that would have choice, Delmarva continues to propose that "all" customers, at the same time, be notified of their right to choose an alternative energy supplier for their "total" facility load up to the limit of each rate class' load for each phase-in year. A lottery would only be necessary, if and when, there was an over subscription of greater than the limit of a rate class electing retail access each phase-in year. This process allows those customers who desire choice to elect choice without being excluded by an initial lottery and provided that the total rate class election is not over subscribed. Delmarva believes that this process also allows for each rate class's load per phase-in year to be achieved in a more efficient and equitable manner. In addition, Delmarva's proposed process minimizes exposure of possible increasing proportional capacity requirement costs by avoiding having to serve only the large commercial and industrial customer's variable load, since such customers, under Delmarva's proposal, must elect 100% of their load to go to choice to be served by one or several alternative suppliers. Delmarva's proposed process also is likely to reduce the number of partial requirement contracts and to reduce their associated daily scheduling and settling administrative costs, compared to Staff's proposed position, since under Delmarva's proposal, not all 700 large commercial and industrial customers are likely to elect a partial requirement contract from one or more alternative energy suppliers over the phase-in period. Delmarva also believes that, for ease of administration and cost control, many customers, alternative energy suppliers and aggregators would prefer to have 100% of each large customer's load go to choice, at one time, rather than requiring partial requirement contracts for every large customer for each phase-in year.

There are other implementation issues that must be resolved, such as customers switching back to a bundled service. These issues need to be resolved as part of the April 1, 1998 filing of unbundled rates or through a separate working group similar to the working group recommended by Staff for implementing consumer education.

3.5 Customer Choice for Municipal Utilities

Please refer to comments under Section 1.3 above.

3.6 The Option of Delaying Customer Choice

STAFF'S POSITION

Staff suggests, as an alternative, delaying retail access to a yet-to-be determined later date. Staff seeks comments on this issue.

DELMARVA'S POSITION

Delmarva believes that any significant delay is not a real option. The Staff report makes two inconsistent points in support of delay. First, the report states that delay would ensure that customers continue to enjoy the benefits of the State's low cost power plants. Second, that delay would enable utilities to reduce, or even eliminate any stranded costs. While Delmarva supplies power to Delaware residents and businesses at rates among the lowest in the region, the Company anticipates that near term competitive supply prices will be lower than those reflected in current embedded-cost retail rates. Stranded costs are created largely by embedded generation costs being higher than the price at which that generation can be sold in the competitive market. Thus, if there are stranded costs that can be mitigated by delay, there is no benefit of delay to customers as they are paying higher embedded costs than they would pay if they had market-priced power available to them.

Further, Delmarva believes that customer choice should not be delayed beyond the time frame needed to logistically provide choice to customers. To delay further would only deny customers the option of exercising their choice of electricity supplier. That choice may be a function of price or any other attribute or combination of attributes. Customers should not be denied or unnecessarily delayed in receiving that basic marketplace freedom.

4.0 The Provision and Regulation of Generation Services

4.1 The Wholesale Market For Generation in Delaware

No comment.

4.2 Market Power

STAFF'S POSITION

Staff's position with respect to the regulation of the generation service is as follows:

- Delmarva will have sufficient market power to hinder the development of the thriving competitive generation market in Delaware.
- The five primary concerns are: transmission, especially load pockets on peninsula; membership in Pennsylvania, New Jersey and Maryland ("PJM") power pool that may favor incumbents; proposed PJM spot market rules that may favor incumbents; incumbents that have an advantage in brand name, customer information; and environmental regulations.
- Many changes will be necessary to overcome the deeply-entrenched monopoly positions of today's utilities.
- The Commission should not consider the transition to a competitive generation market complete until the existing electric utilities can demonstrate that the generation market is workably competitive.
- Federal Energy Regulatory Commission ("FERC") guidelines are insufficient and cannot be used alone to determine market power.

DELMARVA'S POSITION

Delmarva disagrees with Staff's position on market power. The empirical evidence disproves the basis for Staff's market power concerns. In the 1997 merger case before the FERC, Delmarva submitted a wholesale market power study that utilized the FERC's merger guidelines. This study found that, under conservative estimates believed to "overstate the increase in market concentration after the merger," market concentration measures are still well below the FERC's safe harbor threshold.

Delmarva questions the Staff's recommendation to perform two market power analyses during the transition period. The relevant market for analysis includes any generation company that is a member of, or has access to, PJM so that it may market and deliver power to Delaware. This is a very large market with many producers, most of which are larger than Delmarva. Thus, market power issues are unlikely to be of concern in the process of implementing retail access in Delaware.

Below are specific comments on Staff's five primary concerns about market power:

1. **Ownership of Transmission Facilities** - As a transmission owner in the PJM Control Area, Delmarva has empowered the PJM Office of the Interconnection to coordinate and direct the operation of the Bulk Power Transmission Facilities in the PJM Control Area, including Delaware. The Transmission Owners Agreement provides for the coordinated operation, maintenance, and planning of the transmission facilities in the PJM Control Area. The PJM Office of the Interconnection is responsible for directing the operation of the Bulk Power Transmission Facilities in the PJM Control Area. Specifically, the PJM Office of the Interconnection performs the following services for Delmarva as a transmission owner in the PJM Control Area:

    - Develops operating guidelines for the operation of transmission facilities in the PJM Control Area;
    - Coordinates and directs the real-time operation of the Bulk Power Transmission Facilities in the PJM Control Area, including

coordination of outages of Bulk Power Transmission Facilities in the PJM Control Area;

- Administers the PJM Control Area Open Access Transmission Tariff;

- Administers a protocol for Bulk Power Transmission Facilities expansion planning; and

- Performs studies of the reliability and the availability of the Bulk Power Transmission Facilities in the PJM Control Area.

Given the above transmission functions, currently undertaken by the PJM Office of the Interconnection, Delmarva clearly does not have the ability to undertake any actions with respect to its Bulk Transmission System in Delaware which would result in vertical market power.

In addition, Delmarva has completed the expansion of the Red Lion Substation which decisively increases the access of on-Peninsula loads to off-Peninsula generation sources. Under the PJM Open Access Transmission Tariff, Delmarva does not exert any control over the use of any congested path, the pricing of transmission service over the congested path or over the pricing of generation sold over the congested path. Therefore, the combination of the expansion of the Red Lion Substation and the lack of control over congested paths by virtue of the terms and conditions in the PJM Open Access Transmission Tariff, eliminate any concerns about the possible existence of "load pockets" on the peninsula.

2. **Membership in the PJM power pool** - As of August 19, 1997, Delmarva was only one of forty-two members in the PJM power pool. Membership in PJM is open to all qualified electric market participants.

An independent Board of Managers governs PJM. Each PJM member appoints a representative to the Management Committee that advises the Board. Contractual agreements define specific relationships and services provided to PJM market and transmission service participants. The Board of Managers appoints the President who oversees day-to-day operations of the PJM Control Center. Delmarva has no advantage over any other PJM power pool member under the current governance structure of the PJM power pool.

3. **The PJM spot market** - Section 7.01-1.2 of the PJM Open Access Transmission Tariff:

> Cost-based Offers. Unless and until the FERC shall authorize the use of market-based prices in the PJM Interchange Energy market, all offers for energy or other services to be sold on the PJM interchange Energy Market from generating resources located within the PJM Control Area shall not exceed the variable cost of producing such energy or other service.

On July 14, 1997, the PJM Supporting Companies, including Delmarva, submitted a request to the FERC for authorization to make market-based offers for sales through the PJM Interchange Energy Market. This request included materials which demonstrate that the PJM Supporting Companies, including Delmarva, would not be able to exercise market power in the principal relevant geographic and product markets. Currently, the "Cost-based Offers" provision of the PJM Open Access Transmission Tariff eliminates any possibility for generation capacity owners to exert market power.

4. **The advantage of existing utilities historic monopoly position -** Delmarva disagrees with Staff's concerns of the advantages enjoyed by existing utilities and, as stated by Staff, are not a potential exercise of market power.

5. **Inconsistent environmental regulations** - Delmarva believes that the Commission should not dictate environmental policies. This issue is addressed further in Section 11.

4.3 & 4.4 The Default Supplier and the Standard Offer

Staff's position with respect to the need to have a default supplier, especially for small customers, is as follows:

- High cost customers may not have access to the benefits of retail competition;
- The Commission should establish a default supplier to ensure that all customers continue to be provided with generation services at reasonable prices and on reasonable terms;
- The default supplier should have the mandate to seek low cost competitively-priced generation services to the greatest extent possible;
- The default supplier should be required to offer "standard offer" generation services, and the standard offer services and prices would be regulated; and
- Using current assumptions, a standard offer price based on levelized market prices would result in a reduction in Delmarva's current average electricity price of roughly five to ten percent.

In Section 4 of its report, the Staff recommends that the incumbent distribution utility assume the role of default supplier. The default supplier will be expected to serve all customers within a utility's service territory that do not choose an alternative supplier. The Staff expects the default supplier to act as an automatic customer aggregator serving all the customers within the distribution company's existing service territory.

DELMARVA'S POSITION

Delmarva agrees with the Staff's position that a default service provider is necessary and that the present local utility is best suited to offer such a service during the transition period. However, as noted in the introduction to Delmarva's comments, Delmarva strongly disagrees with the Staff's assertion that standard offer generation services be provided at regulated rates In essence, Staff is proposing to deregulate all but the generation capacity required to provide the standard offer services. This would result in a two-tiered electricity market One market would be competitive and the other regulated at the outset of the transition to completion. Delmarva recommends that all generation be deregulated at the outset of the transition to competition.

There are five significant defects in Staff's regulated standard offer proposal:

1. A reduction in the scope of the competitive market;
2. Reduced incentive for efficiency and innovation;
3. Higher costs for the regulated standard offer option;
4. Prices that do not reflect marginal costs; and
5. Lower value received for existing generation capacity.

The following briefly explores each of these deficiencies.

Staff's proposal will eliminate from the market the generation capacity that must be retained to serve customers that desire the regulated standard offer, thereby hampering the development of a vibrant competitive market. Competition provides incentives for firms to be efficient and to introduce innovative products and services. The greater the capacity and number of customers in the competitive market, the more prices will reflect marginal costs. By precluding a significant fraction of generation assets from the competitive marketplace, the Staff recommendation reduces the incentives for incumbent utilities to be efficient and to offer innovative products and services. No regulatory option can replicate the powerful effect of marketplace forces on the efficient allocation of resources.

Another important consideration is that the regulated standard offer will distort the marketplace through the formation of a two-tiered price system. Staff proposes two alternative pricing schemes for the standard offer: a regulated price that "approximates the retail market price," or a "fixed, levelized standard offer price." In the first option, Staff fails to appreciate the fact that there will not be one market price for electricity. Instead, the price consumers pay will reflect cost of serving them. By proposing that a market price be approximated by regulators, Staff is suggesting that the standard offer be used to protect high cost consumers from paying the true cost of service, at the utility's expense. The ultimate result will be what insurance companies refer to as "adverse self-selection." The utility would be left with customers that are, on average, more costly to serve. The Commission will be able to permit price increases to compensate for adverse self-selection only by violating Staff's principle that no customer who chooses the regulated standard offer will be worse off.

Staff's alternative proposal of a "levelized" tariff would dispense with the complexity of attempting to emulate complex market processes in ratemaking. However, this proposal would have the same distortionary effect on retail markets.

The formation of a two tiered price system, coupled with the obligation to serve high cost customers for less than the market clearing price is contrary to many of the objectives of restructuring. First, it violates the prohibition against non-discriminatory rules by requiring utilities to be subject to rules that do not apply to other participants. Moreover, the Staff's proposal does not provide a mechanism for the utility to recover the additional costs associated with being required to serve the high cost customers that are expected to opt for the regulated supply option. Second, the Staff's proposal does not let market forces determine the most effective structure, but instead attempts to restrict the operation of normal market forces. Third, instead of eliminating cross-subsidies as soon as possible, the Staff's proposal perpetuates and possibly increases the magnitude of the cross-subsidies. Another problem with the Staff's proposal is that some customers receiving the regulated supply option are likely to be paying a price that is less than the marginal cost to serve them. The standard offer option will be valuable to customers only if it is below the market clearing price (i.e., the marginal cost of meeting the last unit of demand) and the marginal cost of service. Charging customers a price that is less than the marginal cost of service will cause customers to over-consume and will prevent resources from being allocated to their highest valued use. Setting rates below market levels and below marginal cost will also result in the utility not being willing to make investments to provide safe and reliable service and to meet load growth.

Finally, the Staff's proposal is expected to increase the magnitude of stranded costs. This occurs for several reasons. First, the Staff's proposal is expected to reduce cashflow from generation assets by limiting the price that the utility can charge and by increasing the average cost of service (since the utility is expected to be left with high cost customers). Second, by limiting the utility's ability to release capacity to the market, the Staff's proposal is expected to reduce the incentive for the utility to be innovative and to introduce margin enhancing products. Owners of capacity released to the market will have strong incentives to cut costs, improve performance, and attempt to obtain the highest possible price for their capacity. Consequently, although the price for the generation service may be lower under the Staff's proposal, the total cost (both generation and stranded costs) may actually be higher.

While Delmarva believes that it is appropriate for the incumbent utility to be the supplier of last resort, at least in the short-term, it believes that the price charged for this service should be the market clearing price (plus any administrative cost rec[illegible] to offer this service).

Staff also suggested that Delmarva's current average electricity price could be reduced roughly five-to-ten percent, but fails to supply any support for such determination. Delmarva questions the magnitude of this rate reduction when one consider that Delmarva's prices are already among the lowest in the region.

4.5 Divestiture of Generation Assets

STAFF'S POSITION

Staff recommends that utilities be provided with the flexibility to divest generation assets as they see fit, but only if certain measures are adopted such as standard offer rates, stranded cost reconciliation, sharing gains with customers and the filing of market power studies. Staff also recommends that utilities that do not divest should functionally and financially separate their generation businesses from the transmission and distribution businesses. Staff recommends that such separation be achieved through a transfer of ownership to separate affiliates, but seeks comments on other means. Staff also recommends that utilities file their proposal for separating their generation business in April 1998 in connection with their unbundled rates filing.

DELMARVA'S POSITION

Delmarva disagrees with Staff's linking stranded cost, the pricing of generation and requiring market power analyses to allowing utilities flexibility regarding divestiture. It is Delmarva's opinion that divestiture of generation assets is not necessary nor is the use of affiliates.

In transitioning to full retail customer choice for electric supply, Delmarva envisions the electric business segmenting into three separate businesses: a deregulated energy supply business; a regulated delivery business; and an unregulated energy services business. In fact, the Company has already reorganized into such a separate business unit structure.

Delmarva did this because generation, transmission and distribution services within the industry must be functionally separated in order to move to a fully competitive generation market based on customer choice. However, mandatory divestiture is not desirable or necessary at this time; nor is the mandated use of an affiliate structure. Functional separation is all that is needed to present cross-subsidization.

4.6 Responsibilities of Retail Generation Suppliers

STAFF'S POSITION

Staff recommends that all companies seeking to sell retail electric supply in Delaware should be required to meet certain certification requirements. These requirements are detailed in Section 9.2.

DELMARVA'S POSITION

Delmarva agrees with Staff that all companies seeking to sell retail electric supply services in Delaware should be required to meet certain certification requirements and to adhere to a code of conduct.

It is the Company's opinion that rules and regulations governing the provision of electricity by all suppliers should be established and enforced by the Commission. This could take the form of, or be in addition to, a Certificate of Public Convenience and Necessity ("CPCN"). Such rules and regulations would cover the operations of the supplier to ensure adequate, reliable and safe energy and to ensure that the supplier meets the necessary legal requirements to do business in the State of Delaware.

As examples, the following items should be provided by any supplier of electricity in the State of Delaware: 1) a license demonstrating that the supplier is legally authorized and qualified to do business in the State of Delaware, including all licenses required by the Division of Revenue and by local authorities within the area of proposed operation; 2) evidence supporting sound financial, operational and technical ability to supply electricity within the state; 3) certified financial statements; 4) description of business in Delaware and outside of Delaware; 5) financial and construction plans for all service being offered; 6) experience of operating personnel;

7) description of applicant's engineering and technical expertise; and 8) bonding requirements if applicant requires prepayment for services. These are covered in Staff's recommendations in Section 9.2.

These certification requirements should also require a filing fee. This fee schedule should be commensurate with the actual processing costs so that there is not an impact on the annual Commission assessment levied on utilities in the state.

In addition, each supplier should satisfy several conditions regarding contracts for service, deposit policy, installation and cut-off policy, and other rules of the Commission. All suppliers should also be subject to the same taxes.

5.0 The Provision and Regulation of Transmission Services

5.1 FERC Orders 888 and 889

No comment.

5.2 Implications of PJM's Restructuring for Retail Competition in Delaware

STAFF'S POSITION

Staff recommends that the Commission follow the PJM restructuring process and coordinate the introduction of retail access in Delaware with that process.

DELMARVA'S POSITION

PJM is actively engaged in preparing for retail competition. Through its "Retail Choice Project," the PJM Office of the Interconnection will enable participants in the PJM energy market to conduct business under Pennsylvania's retail choice pilot program. The information system under development by the PJM Office of the Interconnection will offer an internet-based application called "Scheduler" for local distribution companies and load aggregators to provide and obtain information needed to schedule internal transactions under the retail choice initiative. The Retail Choice Information System, which will become operational on October 1, 1997, is being developed by the PJM Office of the Interconnection in coordination with local utility and other PJM market participants. The most recent status report indicated that the project remains on track for an October 1, 1997 operational date. Clearly, PJM is developing the tools necessary to facilitate retail competition within the PJM control area (which includes all of the State of Delaware) and will be ready to accommodate the introduction of retail competition in Delaware in a timely and orderly manner.

5.3 The Role of the Delaware Public Service Commission in Regulating Transmission

STAFF'S POSITION

Staff suggests that reclassifying certain transmission facilities, such as 46 KV lines, as distribution facilities, would transfer costs from FERC rate base to State-regulated rate base. Staff believes that the Commission should carefully consider the impacts on customers of reclassifying transmission facilities as distribution facilities. The Commission should have the authority to regulate retail transmission tariffs, and continue to oversee transmission planning and operation, but Staff seeks comments on this issue.

DELMARVA'S POSITION

Delmarva classifies all facilities 69kV and over as transmission. The costs related to these transmission facilities are included in the development of rates in the PJM Open Access Tariff. To the extent that transmission services are unbundled at the retail level, the unbundled transmission service would be provided under the PJM Open Access Transmission Tariff regulated by the FERC. Delmarva has no transmission facilities below 69kV. Delmarva has 23kV and 34kV distribution facilities; there are no 46kV distribution facilities on Delmarva's system.

Transmission pricing, planning and operations will become FERC jurisdictional issues as indicated in FERC Order 888.

6.0 The Provision and Regulation of Distribution Services

6.1 Responsibilities of the Distribution Utilities.

STAFF'S POSITION

Staff recommends that the distribution utility should be responsible for transmission reliability and least cost planning in addition to the same distribution responsibilities.

DELMARVA'S POSITION

As stated in the Company's comments in Sections 4.2 and 5.3, the PJM Control Area through the PJM Office of the Interconnection will handle transmission reliability and planning subject to FERC jurisdiction. Delmarva agrees that the local distribution utility should have responsibility for distribution reliability, planning, metering, billing and sole authority to connect, disconnect and reconnect customers.

6.2 Ratemaking for Distribution Services

STAFF'S POSITION

The Staff has the following concerns with respect to the use of PBR to regulate distribution services. First, the Staff believes that PBR mechanisms require careful design and implementation, and are difficult to establish. Second, they believe that traditional cost-of-service regulation offers incentives similar to PBR because of regulatory lag. Staff is unconvinced that PBR would deliver consumer protection, market-like incentives, or reduced regulatory oversight as claimed.

As a result, the Staff would encourage the Commission to postpone PBR for distribution services until after the transition period. Staff seeks comments on whether, how, and when various PBR mechanisms could be applied in Delaware.

Staff believes that PBR should encourage efficiency gains and that such gains should be "shared" between ratepayers and shareholders.

DELMARVA'S POSITION

Delmarva disagrees with Staff's position on the ratemaking for distribution services. Delmarva recommends that a PBR price cap plan be implemented for distribution services at the beginning of retail access.

There are two major benefits with the current system of cost of service (COS) regulation. First, being cost-based, it tends to ensure that utilities remain financially viable and are able to supply the quantity and quality of electricity that customers desire. Second, by setting revenues equal to costs, it ensures that the regulated utility does not make excess economic profits.

However, COS regulation has several disadvantages. By linking allowed revenues to costs, COS regulation provides the utility with little incentive to reduce costs. COS regulation also limits the firm's incentive to develop and introduce new products and services. This occurs because COS regulation links the firm's revenues to costs, rather than to the value of the goods and services that are provided to customers. Consequently, COS provides little incentive for the utility to attempt to determine and to develop products that better meet the needs of customers.[5]

Most forms of incentive regulation attempt to break the link between cost and revenues that exists under COS regulation. Under PBR, a benchmark is established and the utility is rewarded/penalized for performance relative to the benchmark. The

[5] In practice, some incentives do exist because of regulatory lag. Regulatory lag occurs because a utility's costs are re-evaluated only at intermittent rate hearing. Consequently, costs reductions are not immediately passed on to the customers in the form of lower prices, but can be retained by the utility in the form of higher earnings until rates are reset.

most commonly used form of PBR is a price cap. With a price cap plan, the utility's **average** price is required to remain below an index price which is adjusted for inflation, industry productivity, and exogenous factors. The index price is designed to mimic the price that would be charged in a competitive market.

Price cap plans have been implemented at both the state and federal level for gas, electricity and telecommunications. Consequently, there is considerable experience with the design of price cap plans, and techniques have been developed for estimating the key price cap parameters.

Some of the key benefits of associated with PBR are:

1. **Productive Efficiency** - It is encouraged both in the utility's direct costs and in its purchases from others Utilities have an incentive to be efficient, because reductions in cost flow to shareholders. Also, the utility's decision-making process is changed to more closely mimic that of a competitive firm. Under traditional COS regulation, capital expenditures increase rates and earnings and thus tend to be viewed in a favorable light. Under PBR, capital expenditures tend to reduce free-cash flow and are therefore viewed in an unfavorable light. As in the case of a competitive firm, capital expenditures should be made only if the risk-adjusted present value of the benefits exceeds the capital expenditure.
2. **Greater Pricing Flexibility and Allocative Efficiency** – Under a PBR program, the utility has greater pricing flexibility than under COS regulation, because it is able to adjust rates in response to market conditions subject to the constraint that the adjusted price does not

exceed the price cap. Under PBR, the utility also has an incentive to adjust rates to ensure that resources are allocated to their highest value use.

3. **Dynamic Efficiency** – It is encouraged because the utility is able to keep increases in revenues resulting from the introduction of new services that better meet the needs of customers. Therefore, compared to other regulatory structures, price cap regulation provides the greatest incentive for the management of a utility to operate the company like a competitive business.

4. **Customer Choice** – This is also enhanced by encouraging utilities to determine the price and quality of service customers desire. PBR can be expected to expand the choices available to consumers, by presenting them with a greater array of services. At the same time, services can be offered at prices which reflect their true market or marginal cost, with attendant efficiency gains. By indicating their preference for some service offerings and not others, the consumers supply the utility the information that it requires to meet market demand. For example, some customers may not require as great a degree of reliability in their distribution service as others, which could lead to the offering of multiple levels of reliability at differing prices.

5. **Regulatory Cost Reduction** – PBR will lead to a reduction in regulatory cost by reducing the need for regulatory record keeping, reporting,

monitoring, and hearings, as well as any costs of defending decisions in court for regulators, intervenors, and utilities.

If properly designed, PBR has the ability to make customers better off, to provide incentives to utilities that are more consistent with those found in unregulated markets, and to reduce the cost of regulatory oversight. However, there are several pitfalls that must be avoided.

1. **Quality of Service Standards** – The basic price cap model does not provide any assurance that the utility will not attempt to increase earnings by reducing service quality. To ensure that this does not happen, price cap plans should include a quality of service mechanism that penalizes the utility for performance that is below some benchmark.
2. **Regulatory Commitment** – A crucial requirement of price cap regulation is the ability of the regulator to live up to the terms of the promises they make. In the economics literature, this is often referred to as the "commitment problem." Generally, neither the utility nor the regulator can bind itself for long periods of time for financial and political reasons, respectively. However, the longer the period of the PBR program, the greater the incentive for the utility to be innovative and to reduce costs.
3. **Social Costs** – PBR plans make it harder to pass on social costs. The utility, like the competitive market, will have no incentive to provide social services beyond what the law or the market requires. As a result,

the imposition of such costs must be explicitly done by legislation or regulation.

4. **Plan Parameters** – Certain judgments are required in the design of good PBR programs. Judgment and analysis is required in the following areas:

   a. Most plans include a measure of inflation. The appropriate measure of inflation will need to be developed and agreed upon. The inflation index is usually taken to be a national inflation index that is reported by a government agency.

   b. Most plans require a productivity offset which must be quantified and agreed upon Productivity offsets are usually estimated using index methods (*e.g.*, Divisia index or Fisher Ideal Index).

   c. The division of risk and the sharing of benefits and costs from the program among stakeholders must be done in a fair and effective way.

   d. The regulators and the utility must resist making premature changes to the bargain. For example, regulators may take back more of the benefits of increased efficiency than had been agreed upon because the utility's success under the initial PBR program was greater than expected (sometimes referred to as "regulatory rebound").

Delmarva believes that a properly designed PBR system will provide the incentives for a utility to reduce costs and to provide the innovative products that customers desire. Moreover, Staff's concerns about reliability and safety can be easily handled by installing mechanisms that penalize the utility for substandard performance. However, as discussed above, it is crucial that the system be designed and administered equitably and fairly and that there be no premature changes to the bargain.

As stated in the Company's Introduction, Delmarva recommends that a Price Cap PBR plan be implemented for the remaining monopoly distribution service at the time that retail access begins.

6.3 Billing, Metering, and Coordination with Alternative Suppliers

STAFF'S POSITION

Billing

Staff recommends:

- Single, consolidated bill from the local distribution company;
- Single, consolidated bill from the alternative energy supplier; or
- Separate bills.

Until billing services become competitive, billing fees charged by the local utility should be regulated. Staff seeks comments on billing matters related to customer choice, pricing for billing services, approaches to ensure proper allocation of partial payments and protocols for allowing alternative suppliers to discontinue service for non-payment.

Metering

Staff recommends:

- The ownership, installation, maintenance, and reading of meters should continue to be part of regulated distribution services, at least during the transition period;
- A generation services provider could supply the customer's meter; and

- Delaware should explore the possibility of increased competition in metering.

DELMARVA'S POSITION

Billing

Delmarva agrees with Staff's position that billing services should remain regulated, at least through the transition period. Delmarva agrees with Staff's position of the three basic billing options suggested by Staff with a clarification that the local utility's charges should only be "calculated" by the local utility during the transition period and that the "total monthly charges" may be sent, upon the customer's directive, to a third party (who may be the customer's energy supplier) for inclusion with the customer's energy charges and one single bill then sent to the customer by that third party. In addition, consideration is being given by Delmarva to provide the customer with a "Not For Payment" copy of the total local utility monthly charges when a third party, other than Delmarva, issues the customer a single bill.

Delmarva is in the planning stage to change its billing system to provide:

- The customer with a single bill which consolidates the customer's local utility's charges and the energy supplier's charges, and
- The energy supplier with meter readings and other billing data.

Staff states that "if one entity is billing on behalf of the other, then the billing entity will need to develop the capability to bill according to the rate design or price structure offered by the other." Delmarva believes that Staff's statement is true when the billing entity "calculates" the other party's charges. However, as another alternative, each party could "calculate" its own total monthly charges and forward electronically such total monthly charges within 24 hours after receiving metered data to the other party or a third party, then one consolidated single bill may be issued to the customer by the billing entity without the billing entity needing to develop the capability of "calculating" the other party's rate design, since the local utility and the energy supplier's total monthly charges may be added together. In other words, when the local utility issues a single consolidated bill, the bill would illustrate the detailed local utility charges added to the energy supplier's total monthly charges without detail; and when the energy supplier or third party issues a consolidated bill, the bill would illustrate the energy supplier charges, possibly in detail, added to the local utility's total monthly charges without detail. When customers have questions about their billing charges, they could be addressed by the party that "calculated" the charge.

Delmarva is planning to offer the customer a single bill service where the energy supplier's total monthly charges will be added to the local utility's detailed monthly charges for a fee to the energy supplier. In addition, Delmarva is considering providing the alternative energy suppliers the capability of "calculating" their energy customer's charges using several standard rate structures for a fee to the energy supplier. Delmarva is planning to determine the appropriate cost of providing both types of billing services and will seek the Commission's approval for such fees at the appropriate time.

With respect to Staff's request for approaches to ensure proper allocation of partial payments to the local utility and alternative energy supplier(s), Delmarva recommends that the local utility should be paid first and then the alternative energy supplier should be paid with any remaining amounts. Delmarva is developing a customer payment posting sequence for the Commission's review. Such a payment posting sequence will identify how the customer's partial payment, toward their single bill, will be prioritized and allocated to the local utility, alternative energy supplier(s) and unregulated value added services. When developing a customer payment posting sequence, consideration should be given to, among other items:

- Regulated versus unregulated amounts due;
- Alternative energy supplier(s)'s amounts due versus value added services amounts due;
- The type or kind of service provided (i.e., energy related versus non-energy related);
- Current amounts due versus amounts due in arrears;
- The length of time of the amounts due in arrears;
- An allocation procedure for customers with multiple energy suppliers with vintage contracts;
- Posting sequence for amounts received for local utilities' deposits versus energy supplier(s)' deposits, if provided for by the local utilities;
- Posting sequence for amounts received the local utilities' extended payment agreements;
- Posting sequence for amounts received for budget plans versus non-budget amounts;
- Posting sequence for amounts received toward goodwill programs, societal programs or state/federal funded energy assistance programs. (i.e., Good Neighbor Program);
- Posting sequence for customer directed and designated amounts received toward specific items;
- Posting sequence for federal, state and local taxes due; and
- Posting sequence for accounts under dispute.

With regards to Staff's request for protocols for allowing the alternative energy supplier to discontinue providing service to a customer, Delmarva proposes that the alternative energy supplier or aggregator should follow the existing Commission's rules and regulations regarding the right to discontinue service. Delmarva proposes that the alternative energy supplier or aggregator should have the right to discontinue the customer's service "contract", once all of the Commission's rules and regulations are met. Delmarva firmly believes that the alternative energy supplier or aggregator should not have the right to disconnect electric service to a customer for any reason. Delmarva's current rules and regulations regarding discontinuance of service may be found in Delmarva's Electric tariff, Section XV, leaf numbers 27-28a.

Metering

Delmarva agrees with Staff's recommendation that the distribution utility should continue to own, install, maintain and read meters, and strongly recommends that it stays that way. Staff's suggestion that the Commission, at some point, require that certain metering services be provided on a competitive basis deserves additional comment. First, regulators and policy makers should be concerned about the potential for coordination problems. Second, it has long been recognized that there are significant economies of both scale and scope in the provision of metering services. Finally, the structure of the metering services market will also have an impact on stranded cost recovery.

Coordination Problems

There are expected to be many coordination problems associated with unbundled metering. If independent firms are not properly integrated with electric supply services, there may be serious coordination problems in the implementation of new metering systems. Accurate and efficient billing can occur only if metering information is provided on time, free of errors, and in usable form. If many different metering companies must send information to many different billing companies, the possibility of delays and errors increases. Furthermore, coordination problems in the competitive provision of metering could lead to significant problems with settlement, load imbalances, and other serious issues that might affect both the settlement process and system reliability.

The experience in the United Kingdom proves this point. The United Kingdom implemented retail access in 1994 with competition in the provision of metering services. However, the U.K. has experienced significant coordination problems as a result. Customers who had contracted for advanced metering systems did not always receive them in a timely fashion, and many of the new meters that were installed were not properly connected to the data collection network. In the first six months, usage for over 50 percent of the customers that had signed up for new metering systems was not properly recorded. As a result, bills for these customers had to be estimated. There were problems with load imbalances and the distribution companies' cash flows suffered considerably.[6]

Safety is another concern that the Commission must consider. Delmarva has strict standards regarding meter quality and installation. Open competition could pave the way for inferior "offbrand" metering equipment being installed by poorly trained

[6] Henney, Alex, "Competition, Confusion, and Chaos: The Metering Muddle," Public Utilities Fortnightly, 134:20 (November 1, 1996), pp. 26-29.

technicians. An inferior meter and/or installation could put the residence and part of the distribution system in jeopardy. Obtaining access to a meter not owned by the utility could also pose additional problems for the local utility during emergencies.

Economies of Scale and Scope

As the sole provider of meters, the local utility can realize greater economies by purchasing on behalf of all customers than could several service providers. Once the utility has obtained the meters, it can then exploit the economies of scale or density in the installation of meters in a given geographic area. Having a single firm install and read meters in every home in a neighborhood will require fewer resources than having several firms install and read the meters. As an example of the economies of dens. consider on-site meter reading. A meter reader who reads every meter in a consecutive path will read 10 times more meters than one who reads every 20th meter.[7]

The traditional method of data collection, on-site meter reading, requires large investments in personnel and fleet services. Advanced methods being tested today are expected to lower the cost of data collection significantly. The advanced methods require connecting the meters on the customer's premises to the central data processing unit by a data communications network. While the choice of network – e.g., wireless or wireline – will influence the cost of service, the fixed costs remain large. However, once the network is brought to a neighborhood, the cost of serving additional customers in the area is very small. In other words, the marginal cost of

[7] King, Chris S., "Competition at the Meter: Lessons from the U.K.", Public Utilities Fortnightly, 134:20 (November 1, 1996), pp. 22-25.

service is less than the average cost, and adding additional customers to the network will lower the average cost of service to all customers.

The California proceedings provide compelling evidence of the dramatic economies of scale from widespread implementation of advanced metering. Estimates of the cost of providing metering service to small California customers in a multi-firm market vary widely—from a high of $27 per meter per month, to a low of $5 per month—based on assumptions of between 5 and 10 percent penetration.[8] On the other hand, Cellnet Data Systems, a leading provider of advanced metering technologies, has estimated that a saturated deployment of advanced metering would cost as little as $1 per meter per month for small customers. Thus, the minimum cost savings from exploiting economies of scale would be 5 times and the maximum might be as high as 27 times.

Stranded Costs

Allowing competitive firms to provide metering would substantially complicate stranded cost recovery. With competitive providers of metering, the Commission will need to revisit the issue of stranded cost recovery (in the context of metering). The cost of existing metering no longer being used for billing will need to be recovered. Moreover, to the extent that customers opt for other metering providers, the utility's average cost of providing metering is likely to increase relative due to lost economies of scale and scope.

The Staff proposal would allow customers or other suppliers to provide the distribution company with an upgraded meter. As described above, there are

[8] These figures represent total cost of service, including network infrastructure costs, meter acquisition and financing, and data collection costs.

substantial and compelling reasons to maintain monopoly provision of metering services. By allowing other suppliers to provide meters, the Commission is inviting a host of coordination problems and potential anti-competitive behavior. For example, other suppliers could tie service contracts to the purchase of a meter. Alternatively, as discussed above, the compatibility factors are so numerous as to make the establishment of a truly "open" architecture unlikely, even under the best of conditions. Such outcomes would have a decidedly negative effect on the transition to competition in Delaware. Therefore, Delmarva strongly recommends that the Commission continue its present policy of regulated metering services.

7.0 The Unbundling and Pricing of Electricity Services

7.1 Benefits of Unbundling

<u>STAFF'S POSITION</u>

Staff presents a number of benefits associated with providing major services to all customers on an unbundled basis. Staff recommends that utilities file proposed unbundled rates, along with supporting documentation by April 1, 1998. The unbundled rates would go into effect on January 1, 1999.

<u>DELMARVA'S POSITION</u>

Delmarva has already presented a preliminary draft of an unbundled rate design, complete with detailed documentation. There is no need to delay the filing of an unbundled rate design until April 1, 1998. A complete unbundled rate filing, based on a December 31, 1996 ending test year, could be provided to the Commission by December 1, 1997. Staff's recommendation to delay an unbundled rate filing until April 1, 1998 would still, given data constraints, require the use of a December 31, 1996 ending test year. A complete unbundled filing, based on a December 31, 1997, ending test year would not be available until May 29, 1998. Staff and other intervenors are already familiar with the unbundled rate design concepts and detailed supporting documentation provided to them, based on a December 31, 1995 test year.

7.2 Revenue Neutral Unbundling

<u>STAFF'S POSITION</u>

Staff believes that a balance must be struck between offering a wider range of choices for individual services and providing a bundled offering which some customers may prefer. Staff also believes that services must be unbundled and priced on a revenue neutral basis. Staff wishes to have customers pay the same rates irrespective of whether services are unbundled our bundled. They explicitly object to unbundled rate designs that will increase the access charge and lower the usage rate, since these rate designs will cause customers to pay more for the service if consumption should fall.

DELMARVA'S POSITION

Unbundling of retail rates should be used as an opportunity to move rate classes and individual rate elements closer to the costs of providing these services to customers. In some cases, this may result in the shifting of revenue responsibility between rate classes or among customers within a rate class. The detailed documentation already provided by Delmarva supplies the information necessary for the Commission to evaluate the unbundled rate elements. Proper price signals are a necessary part of a vibrant and dynamic retail choice option for customers in Delaware. To provide the proper price signals the usage rates for unbundled services should be set as close to the marginal cost of providing the service as possible and fixed costs should be recovered through an appropriate mechanism. The mechanism selected should ensure that the utility's fixed costs are recovered across all services, economic efficiency is enhanced, and competition is recognized at both the bundled and unbundled levels. Failing to adequately address the appropriate price signals will result in unbundled retail rates which do not provide customers with adequate cost information that their choice and usage decisions impose on other retail customers in Delaware.

7.3 Principles of Unbundling

No comment.

7.4 Unbundling the Costs of Retail Generation Services

STAFF'S POSITION

Staff supports the accurate unbundling of all cost components of retail generation services.

DELMARVA'S POSITION

Delmarva agrees that all of the costs associated with retail generation (electric supply) service should be included in the unbundled rate. The costs associated with ancillary services, whether transmission or generation related, should be recovered as a separate unbundled rate element from generation capacity and energy costs. These ancillary services are distinct services provided to unbundled customers under the PJM Open Access Transmission Tariff. Delaware does not have a gross receipts tax on utility service, but there is a public utilities tax that should be included in the unbundled rates.

8.0 Estimation and Treatment of Stranded Costs

8.1 Definition of Stranded Costs

STAFF'S POSITION

Staff defines stranded costs as the portion of a utility's generation assets that exceed the market value of the generation services available from those assets. Staff classifies these costs as generation assets, generation liabilities, and regulatory assets. Staff recommends that Delmarva file an estimate of its potential stranded costs by July 1, 1998.

DELMARVA'S POSITION

Delmarva agrees with Staff's definition of stranded costs, but is concerned with the categorization of nuclear decommissioning as a regulatory asset. Unlike regulatory assets, which represent incurred costs deferred for future recovery, nuclear decommissioning costs are future expenditures being funded in the present, as the Nuclear Regulatory Commission, State Commissions, and FERC have mandated. In a sense, nuclear decommissioning is similar to the future demand-side management program costs, which Staff has recommended be removed from stranded costs and instead recovered through a societal benefit charge. Similar to the societal benefit charges, nuclear decommissioning is a long-term funding commitment. Sufficient funding of nuclear plant decommissioning trust funds is critical to the public health and safety, and it is Delmarva's position that all customers continue to contribute to these funds.

8.2 Methodology and Principles for Estimating Stranded Costs

STAFF'S POSITION

Staff defines two broad approaches for estimating stranded costs: Market Valuation, which uses auctions, sales, or asset spin-offs, and Administrative Valuation, which uses forecasting, modeling, or other analytical tools. Staff recommends that Delmarva use an administrative valuation approach to prepare a stranded cost estimate by July 1, 1998 and suggests the following principles be applied:

- Stranded costs be estimated on a net, system-wide basis;
- Stranded costs estimates include individual plant assessments;
- Estimates should account for forecast changes (in both market prices and asset value), with a study period no shorter than 15 years; and
- Sensitivity analysis be performed, including variations in market prices and other key assumptions.

DELMARVA'S POSITION

Delmarva agrees that an administrative valuation approach is the most acceptable one and agrees that a limited number of reasonable sensitivities is advisable.

8.3 Potentially Strandable Costs and the Link to Standard Offer Prices

STAFF'S POSITION

- Staff believes that stranded costs should be estimated based on what they term potentially strandable costs
- Potentially strandable costs are estimated by assuming that the utility is able to charge only the market price for all of its generation output.
- Staff believes that ideally the standard offer prices should be linked to strandable costs in the sense that both should be based on market price.
- During the transition period, Staff recommends that the standard offer price continue to be regulated and be capped at the generation price that is currently charged in today's bundled electricity rates.

- The standard offer price should include the retail cost of generation plus additional costs such as the cost of reliability, marketing costs and A&G costs.

DELMARVA'S POSITION

Delmarva is not clear about Staff's positions and definitions regarding potentially stranded costs and actual stranded costs likely to be incurred, and their link to the standard offer price. Under the Staff's proposal, it is expected that the standard offer rate will be equal to the cost-of-service rate currently charged in today's bundled electricity rates. Delmarva's position is that such a standard offer price is not appropriate. (This is further discussed in Section 4.3.) A standard offer rate based on regulatory rules, combined with stranded costs calculations based on market prices, would indeed result in the discrepancy between the potentially stranded costs and actual stranded costs that Staff envisions.

Delmarva's proposal included a "standard offer rate" based on the frozen 1998 tariff price (adjusted for the MTC). Delmarva believes this approach is reasonable and appropriate for the following reasons:

- The offer price remains stable over the transition period, which is attractive to consumers during an uncertain time; Delmarva assumes the fuel and market risks during the transition period; and

- The Commission does not need to oversee or adjust the standard offer rate during the transition period.

If, however, the Commission determines that another form of standard offer price is appropriate, Delmarva believes it should be based on the market price, and not regulated; there should be consistency between the assumptions underlying the standard offer rate and the stranded costs. To this end, Delmarva would propose calculating the generation-asset stranded costs by subtracting the assets' estimated future costs from their projected market revenues; this difference would then be compared to the assets' book value. Similarly, the standard offer price would be based on the market price, with additional administrative costs taken into account. Because no significant divergence is expected between actual and projected market prices during the transition period, this approach is compatible with Staff's apparent objective of maintaining consistency in the approaches.

8.4 Determining Which Costs Are Eligible for Stranded Cost Recovery

STAFF'S POSITION

Staff recommends that utilities be required to mitigate stranded costs and efforts should focus on cost reduction measures; other options Staff does not support are cost shifting and revenue enhancement. Staff also suggests that recovery should not be guaranteed and that the Commission should evaluate whether certain stranded costs should be borne by stockholders; this would be determined after reviewing the utilities' stranded cost filings to be made in July 1998.

DELMARVA'S POSITION

Delmarva believes strongly that non-mitigated stranded costs should be allowed for full recovery. Delmarva agrees that stranded costs should be mitigated to the extent possible; for example, savings related to the imminent merger with Atlantic Energy could be used to offset stranded costs. In addition, flexibility should be allowed with regard to the different options outlined by the Staff.

Delmarva objects to accelerating depreciation because the Commission has previously approved certain depreciation rates, and acceleration of these rates shifts the burden to the shareholders by lowering earnings per share. However, Delmarva would be willing to entertain a such a mitigation strategy, with the condition that it be revenue-neutral.

In general, Staff's position on the "sharing" of stranded costs raises serious questions. Absent a showing of waste, bad faith or abuse of discretion, stockholders should not bear any portion of these costs.

This can best be explained by the phrase "obligation to serve". The Company has had the obligation to provide electric power to its customers, and its customers have had the right to expect that the Company would provide this service in a safe, adequate, and reliable manner. Historically, this was accomplished through providing exclusive retail service franchises. For the Company, this means that investments have been made in order to serve every one of its customers in its DPSC delineated service territory. The Company did not have a choice of who it could serve, or to serve only those customers who provided the best return on investment. Delmarva's responsibility has been met through long-range planning and through the continued investment in sufficient generation, transmission, and distribution resources. In return for this investment and level of commitment, the Company has been statutorally provided the opportunity to earn a fair return on its investment. That return was set using the assumption that the Company would continue to have the opportunity to earn that fair regulated return on its investments. These arrangements, and corresponding obligations, are generally what is meant by the "regulatory compact" concept.

Delmarva's own generating stranded costs represent investments made to provide a safe, adequate and reliable electricity supply to serve our customers' needs and fulfill our statutory obligation to serve. Investors expected, and continue to expect, a reasonable return on, and of, their investment. Under the regulated monopoly structure, that is what they received, and by law, were entitled to receive. As the industry is restructured to provide for retail choice, these investors must be compensated for their good faith investments in the infrastructure of Delaware through their investment in Delmarva.

8.5 Recovery of Stranded Costs Through a Market Transition Charge

STAFF'S POSITION

Staff recommends recovery of stranded costs through a MTC. The MTC would be charged separately from other unbundled electricity rates and would be applied to all transmission and distribution customers on a non-bypassable and non-discriminatory basis. Staff recommends that the charge be collected during the four year period, April 1, 1999 through April 1, 2003. The MTC is to be collected on the basis of energy usage (i.e., per kWh).

DELMARVA'S POSITION

As noted previously, Delmarva agrees with Staff that stranded costs should be collected through a non-bypassable charge applied to all transmission and distribution customers, although Delmarva believes all stranded costs should be recovered, not just those the Commission deems "significant". This ensures that all suppliers will pay the transition costs associated with the new regulatory regime, including stranded costs, since all customers will require transmission and distribution services.

Delmarva has concerns with some of the other aspects of Staff's proposal. First, Delmarva believes that stranded costs should be allocated to the rate classes based on cost causation, and then the appropriate MTC determined for each customer class. Second, Delmarva believes that the MTC should be collected as an access fee (i.e., a fixed amount per month), instead of on a per kWh basis. Assessing it on a per kWh basis will distort the price signal for the distribution service. To enhance economic efficiency, the usage rate should be set as close as possible to the marginal cost of providing the distribution service. Third, attempting to collect the MTC on a per kWh basis will increase the uncertainty in the estimate of stranded costs, since it will be necessary to have accurate estimates of energy usage (in kWh).

Finally, while a four-year recovery period may be appropriate for the majority of the stranded costs, Delmarva suggests that the recovery of the nuclear decommissioning costs be extended to the end of nuclear plant lives.

8.6 Reconciliation of Stranded Costs Over Time

<u>STAFF'S POSITION</u>

Because of the uncertainty associated with estimating stranded costs fifteen years or more into the future, Staff recommends that there should be a reconciliation between stranded costs recovered and stranded costs actually incurred. Staff recommends that the Commission conduct a review of stranded cost recovery by January 2003. The policy review is to be limited to a comparison between actual stranded costs and those recovered through the MTC. If the Commission finds that actual stranded costs deviate from those recovered by more than 25 percent, then the MTC should be adjusted and the collection period extended beyond January 2003.

DELMARVA'S POSITION

Delmarva believes that it is unnecessary to reconcile recovered stranded costs with actual stranded costs by January 2003. Given Delmarva's cost structure, the Company believes that the magnitude of stranded costs in general and the forecast error (at the beginning of 2003) in particular is not expected to be significant. The real uncertainty in the value of the generation assets is expected to occur after the end of the transition period, and any differences between projected and actual market prices in the first four years do not dictate the nature of such differences in future years.

While this would argue for the reconciliation to occur later than 2003, Delmarva believes that stranded cost payments should end after the termination of the transition period. A more accurate reconciliation would not be possible until the end of the assets' lives, because the true market prices will of course be unknown until they occur; in some cases, this is approximately 30 years from now. Delmarva believes such a reconciliation is unreasonable and overly burdensome; Delmarva is willing to assume the financial risks associated with no reconciliation.

However, if the Commission decides to reconcile recovered versus actual stranded costs as the Staff has recommended, then Delmarva believes that it is imperative that an objective mechanism be established beforehand. Otherwise, Delmarva is concerned that there will be a temptation to reduce but not to increase the MTC if actual conditions differ from those forecast.

One way to objectively reconcile recovered and actual stranded costs would be to use an index methodology which could be applied to the initial estimate of stranded costs. The index would be based on the key drivers of electricity prices, such as fuel costs, heat rates and installed costs for new generation units.

When properly constructed, the stranded cost index would rise and fall in parallel with electricity prices. When the index rises (indicating that stranded costs are less than expected), stranded cost recovery would be lowered. When the index falls (indicating that more stranded costs must be collected than originally forecast), stranded cost recovery would be increased.

The index methodology begins with an initial level of stranded costs that reflects expected conditions with respect to the key drivers of electricity prices. The initial estimate of stranded costs would be adjusted based on differences between base assumptions and actual market levels at the end of 2003.

A key benefit of an index method is that it provides an objective means of adjusting for differences between recovered and actual stranded costs. This should help to ensure a fair and objective process in which the estimate of stranded costs would be increased, as well as decreased, if actual conditions deviate from those forecast.

8.7 Stranded Costs for the Cooperative and Municipal Utilities

No comment.

9.0 Consumer Protections and Equity

9.1 Customer Aggregation

No comment.

9.2 Standards for Retail Electricity Sellers

<u>STAFF'S POSITION</u>

Staff recommends that aggregators be required to meet certification and bonding requirements, adhere to a code of conduct, and fulfill the operational provisions specified by distribution companies and the regional ISO. Staff also recommends that certified providers *should* be required to update certification information annually and be subject to Commission audit.

<u>DELMARVA'S POSITION</u>

Delmarva supports Staff's recommendations and provides further comments on this issue in Section 4.6. Staff's certification requirements are also appropriate. Delmarva believes that the "defaulted provider" should acquire the power at the prevailing market price.

9.3 Low-Income Customers

<u>STAFF'S POSITION</u>

Staff recommends that low-income customers continue to be provided energy efficiency services and that the Commission establish a supplier of last resort so that the obligation to serve is retained. Staff seeks comments on implementing low-income bill assistance programs.

DELMARVA'S POSITION

Delmarva does not believe that existing low-income programs should be enhanced. Low-income customers should ultimately receive the same benefits of retail competition as other customers receive. Benefits to low-income customers would likely include lower energy prices, and more choices and more options that may be beneficial to them, such as a variety of credit and payment plans. All customers should still be subject to reasonable disconnection policies for non-payment of bills.

Delmarva has a strong track record with low-income assistance programs. Delmarva currently supports such programs as the Low Income Energy Assistance Program ("LIHEAP"), and the Good Neighbor Energy Fund. Delmarva also administers several bill assistance programs, where customers are able to negotiate customized payment plans to meet their needs. One particular program, in cooperation with local churches and other Community organizations, allows customer accounts to be extended indefinitely when they are targeted to receive funds. Delmarva also offers a Budget plan whereby customers are billed a levelized amount based on annual usage.

This type of a public policy program is an issue that may be better addressed by the General Assembly. What Staff is suggesting is, for the most part, another tax. If this is the appropriate public policy for the State of Delaware, then Delmarva supports the notion that the funding should be supported by all participants.

9.4 Consumer Education

STAFF'S POSITION

Staff recommends that all stakeholders play a role in consumer education and that marketing materials and bills be required to conform to a standardized format. Staff also recommends that payment schedule, disconnection procedures, and dispute resolution procedures be disclosed to customers both on educational materials and on their bills. Finally, Staff recommends that consumers be informed that they have the right to prevent their distribution utility or other alternative supplier from releasing their personal information (e.g., *name*, address, etc.) as well as data about their payment history, specific usage patterns, and appliances. Staff suggests that a working group be established to address the implementation of these recommendations.

DELMARVA'S POSITION

Delmarva agrees with Staff that many players could and should play a role in educating consumers about customer choice, and that the distribution utility should play a key role in such efforts by using its communications expertise, relationships with external groups, and existing channels of communication. Delmarva further agrees that a working group should be established during the first quarter of 1998 in order that initial communications and education efforts can begin as soon as possible after restructuring is ordered.

In this regard, Delmarva suggests that the following guidelines be utilized:

- Communication should be timely;
- Communication should be presented in easily understood language;
- Communication should be unbiased, objective, and fair;

- Communication should be made accessible to all consumers by using a mix of communication vehicles to reach the intended audiences including employees, consumers (both individual consumers and groups or associations), and the media;

- Education efforts should continue throughout the transition period;

- Education efforts should be clearly separated from marketing and sales efforts;

- Public opinion research should be conducted to measure the effectiveness of communication and education efforts, and to aid in refining the messages and planning continuing efforts; and

- The author or presenter of information should be clearly identified so consumers can assess message credibility.

Staff has also recommended the establishment of a standard bill format, and Delmarva is willing to explore that idea with the other parties. With respect to the distribution of marketing materials, however, Delmarva is concerned with Staff's proposal to adopt a standardized approach

In Delmarva's view, a standardized approach for marketing is too rigid and inflexible, and a one-size-fits-all approach assumes that all customers want and need the same information. As a result, it would create the following problems:

- Customers would get far more information than they actually want/need, creating much confusion;

- Customers would perceive that marketers are attempting to be all things to all people and are not flexible and understanding of their needs;

- Marketers and suppliers would be discouraged from investing in products/services/enhancements outside of industry standards;

- Industry would decide what is important to customers instead of research/discussions with customers by marketers; and

- Targeted communication and offers to customers would be discouraged.

10.0 Resource Planning, Energy Efficiency and Renewable Resources

10.1 Achieving the Objectives of Integrated Resource Planning

STAFF'S POSITION

Staff believes that many of the fundamental objectives of integrated resource planning ("IRP") are still important in a competitive electricity market. Staff recommends:

- That the default supplier evaluate a wide range of generation supply options;
- Continue cost-effective energy efficiency programs through the distribution companies; and
- Reduce environmental impacts through promoting renewable resources, green power and encouraging comparable environmental requirements.

Staff also seeks comments on the appropriateness of reporting requirements for trends in reliability, transmission needs, resource diversity and impacts of competition.

DELMARVA'S POSITION

Delmarva cannot support Staff's recommendations. Delmarva believes that existing IRP guidelines should be modified or eliminated now. Certainly, once effective competition for generation has emerged in Delaware, existing IRP requirements should be eliminated. It would be impractical to impose an IRP requirement on generation when electricity is traded as a commodity in competitive markets. Additionally, the long-run planning perspective of IRP is of little value to individual suppliers.

Much of the information the utility must provide in compliance with the present IRP regulation is commercially sensitive. In addition, there have been instances in which people have misused or misinterpreted information contained within Delmarva's IRP.

Delmarva believes that once retail access arrives, customers will decide, through their purchasing decisions, on the appropriate level and types of demand-side management ("DSM") and energy efficiency programs that they wish to pay for. These DSM programs will be offered by energy suppliers and/or service companies formed for this purpose. There will be no need for regulators to perform this function.

Delmarva also believes that competition should provide price signals to customers which reflect the marginal costs of suppliers, and consequently renewable resources and other "clean" generation resources that are economical will have an advantage over "dirtier" generation resources that have to comply with ever more stringent environmental requirements. As such, Delmarva does not see the need for promoting renewables.

With regard to recommending that all suppliers be required to prepare biennial reports on trends in reliability, transmission needs, resource diversity and impacts on competition, Delmarva does not believe that this additional reporting is necessary in competitive market. The Commission should be attempting to remove regulatory barriers to entry and to streamline or reduce reporting requirements. Reliability issues are further addressed in Section 10.2.

10.2 Resource Planning at the Distribution Level

STAFF'S POSITION

Staff believes that distribution companies should continue to have the responsibility to provide low-cost, reliable, efficient and safe transmission and distribution services.

Staff recommends that the distribution utility should be required to perform a modified version of IRP, sometimes referred to as "integrated distribution planning" ("IDP"), with a focus on lowering T&D costs and improving "T&D" efficiency.

DELMARVA'S POSITION

As discussed in Section 6.2, Delmarva believes that Staff's objective can be accomplished by implementing a correctly-designed PBR plan. As discussed in that section, the advantage of a PBR plan is that it provides a stronger incentive for the utility to be efficient and innovative than traditional cost of service regulation. The utility has a clear incentive to pursue all measures, including integrated distribution planning, designed to reduce costs and improve efficiency. Also, concerns about service quality and safety can be handled under a PBR system by implementing safety and quality performance mechanisms that penalize the utility for inferior performance. Delmarva believes that a properly designed incentive system will be able to accomplish the Staff's objectives for less cost than under traditional COS regulation, especially since regulatory oversight will be greatly reduced.

In any event, transmission is FERC-jurisdictional and should not be included in State-level resource planning.

10.3 Promoting Energy Efficiency Investments

STAFF'S POSITION

Staff is concerned that relying solely upon the market to deliver energy efficiency services will leave a large portion of cost-effective energy efficiency resources untapped. The Staff recommends continued Commission oversight and that the Commission establish a system benefits charge ("SBC") to raise revenues to finance energy efficiency services. The SBC should be charged to all customers served by each distribution company, regardless of their generation service provider, i.e., it would be non-bypassable. The Staff also recommends that the SBC be administered by an independent, non-profit or public agency. Finally, a portion of the SBC funds should be set aside to finance energy efficiency programs for low-income customers.

DELMARVA'S POSITION

Delmarva agrees that energy efficiency and peak management programs have been important benefits to consumers in the state. However, Delmarva disagrees with the adoption of a system benefits charge to fund these programs. Depending on the nature and amount of this charge, its imposition could affect the competitiveness of the rates charged in Delaware versus other states in the region. In addition, Delmarva believes that, under full retail competition, consumers will ultimately select the most efficient type and amount of energy efficiency program to continue. A separate charge to fund these programs could have the effect of subsidizing programs that could be maintained in an unrestricted market.

In addition, the establishment of an SBC will most certainly result in increased prices to customers to support these programs. This appears to be a contradiction to Staff's position that customers should be no worse off.

10.4 Promoting Renewable Resources

STAFF'S POSITION

Staff recommends that the Commission establish a renewable portfolio standard ("RPS") that would be applied to all suppliers seeking to sell power in Delaware. Staff also recommends that the Commission establish policies to support research and development ("R&D").

DELMARVA'S POSITION

Delmarva does not support Staff's position. Delmarva has been active in investigating, developing and demonstrating potentially cost-effective uses of renewable energy for more than twenty-five years. The Company is presently actively working with several business partners and the United States Department of Energy in developing a cost-effective, dispatchable, peak-shaving photovoltaic system for commercial building application. Presently, systems are installed at: the Carvel State Office Building in Wilmington, Delaware; Delmarva's Northern Division General Office Building in Newark, Delaware; and in Maryland, North Carolina, and Wisconsin. Delmarva has also installed two of these photovoltaic systems to provide educational opportunities to Delawareans at the Delaware Nature Society's facility in Abbott's Mill and at the Hockessin Montessori School. In Autumn, 1997, another system will be installed at the Delaware Division of Facilities Management's office in Dover, Delaware.

All of the above efforts were accomplished without any regulations requiring such action. Accordingly, Delmarva fully supports the practice of promoting renewable resources for generation, but is opposed to Staff's recommendation of a "renewable portfolio standard" whereby suppliers would be required to maintain a target mix of generation resources.

As retail customers are provided choice as to their energy supplier, the range of choices that are afforded them will increase dramatically. Artificial barriers to market entry for renewable resources will be removed. It is Delmarva's expectation that some suppliers will market themselves to customers partly on the basis of their source of supply; e.g., non-nuclear sources, wind and solar energy only, or hydro power. This occurred in the recent New Hampshire pilot program.

Competition should provide price signals to customers which reflect the marginal costs of suppliers and, consequently, renewable resources and other "clean" generation resources that are economical will have an advantage over "dirtier" generation resources that have to comply with ever more stringent environmental requirements.

11.0 Maintaining Environmental Quality and Comparability

11.1, 11.2 & 11.3 - Threats to the Environment, Promotion of Green Power and Policies to Encourage Comparable Environmental Standards

STAFF'S POSITION

Staff is concerned with inconsistent environmental standards and proposes:

- Electricity sellers should be encouraged to provide customers with the choice of green power, and required to disclose the emissions associated with their power supply (Section 11.2); and
- The Commission and environmental regulators in Delaware should devise policies to promote greater comparability in environmental standards applied to electricity sellers in Delaware (Section 11.3).

The Staff points out that the Commission is not responsible for establishing environmental standards. Rather, that responsibility rests with other state and federal agencies. Nonetheless, Staff is seeking comments on mechanisms for promoting comparable environmental standards across suppliers in Delaware.

DELMARVA'S POSITION

Delmarva disagrees with Staff's position on this issue and believes that environmental labeling disclosure and policies to promote environmental comparability should not be mandated by the Commission. Delmarva recognizes that there is continued uncertainty in accurately predicting and assessing any potential environmental impacts (both positive and negative) associated with electric utility restructuring. Delmarva believes that environmental matters should continue to be handled by the appropriate state and federal agencies, such as the Delaware Department of Natural Resources and Environmental Control ("DNREC") and the United States Environmental Protection Agency ("USEPA"), through existing statutes, regulations, permits and rulemakings. These agencies possess the technical expertise to determine, what, if any, regulations need to be promulgated on a local, regional or national basis in order to ensure environmental protection and the avoidance of any significant deleterious environmental impacts associated with any new initiatives.

Furthermore, if the retail markets for electricity are to be allowed to become customer-focused and economically efficient, careful attention should be paid to any proposal that would compromise the efficient operations or viability of the competitive market. The regulation of competitive markets is only appropriate when there is need to address a failure in the market itself. The use of regulation to augment the efforts of state and federal air quality regulators should only be employed after it has been demonstrated that (1) there is a failure in the marketplace and (2) the imposition of regulation is the most economically-efficient means for addressing the market failure.

As an alternative to the premature or improper imposition of environmental requirements on the electric markets in Delaware, Delmarva encourages the Commission to adopt a competitive framework that will facilitate, rather than require, the development of energy "products" that capitalize upon the interest of consumers in environmental issues through the use of voluntary product development and disclosure, and the use of uniform educational tools. Although this will clearly require a commitment upon the part of the state and its licensed retail suppliers to provide consumers with appropriate educational tools, it will generate a broader awareness of the industry, its economics and the actual impact of electric generation upon the environment. It will also provide an economically-efficient mechanism for promoting renewable generation and cleaner power resources without creating a barrier to the practical operation of retail and wholesale electric markets. As a result, Delaware will be the beneficiary of both the environmental and economic benefits of a *truly* competitive marketplace.

Delmarva also offers the following specific comments with respect to Staff's recommendations associated with Emissions Labeling and Disclosure, Generation Performance Standards and Implementation of New Source Performance Standards on pre-1971 generating facilities:

Environmental Labeling and Disclosure

Delmarva believes that environmental labeling and disclosure information does not need to be mandated by the Commission in order for consumers to make informed decisions regarding generation supply choices. Rather, Delmarva believes that labeling and disclosure should be encouraged to be performed by electric suppliers on a voluntary basis. Customer choice will dictate whether or not this information is valuable in making energy purchase decisions. Should environmental labeling and disclosure information be desired by customers, responsible energy providers would be motivated to voluntarily provide the information in order to harness market-based business opportunities.

In determining the parameters to be disclosed under any voluntary program, a uniform, national and/or regional approach is needed. A broad array of environmental attributes should be considered across all media. For example, while the emission characteristics of certain air pollutants could be considered for fossil fuel fired plants, equal consideration is necessary regarding the potential aquatic impacts associated with hydroelectric generation. Likewise, hazardous and radioactive waste considerations should be disclosed from nuclear powered facilities. The public should be given a balanced picture of all major environmental attributes, and not just one or two indicators. These attributes should be uniformly defined and consistent across political jurisdictions to ensure that gaming does not occur.

Comparable Environmental Standards

Delmarva strongly believes that the Commission should not dictate environmental policies to promote environmental comparability standards for electric sellers in Delaware. Delmarva believes that a Generation Performance Standard ("GPS"), or the imposition of New Source Performance Standards ("NSPS") on generating units built prior to 1971, could have severe economic impacts for any states that adopt such measures unilaterally.

The implementation of a stand-alone generation performance standard for NOx - a pollutant of concern identified in the Staff' report - would provide an unknown benefit, and could even provide ambient ozone disbenefits. Any standard that would require retail suppliers to have to accurately and verifiably procure resources with specific generation attributes would also impose an economic and legal burden upon suppliers that will discourage competition and generate market failures that will result in higher energy prices that would otherwise be available to customers. Moreover, as noted below, the development of a GPS or NSPS requirement on older units in Delaware could have a detrimental economic impact, without necessarily providing commensurate environmental improvements in Delaware or other nearby states.

It has been scientifically demonstrated that the emissions of NOx from major sources (utility, industrial and mobile) along with the emissions of Volatile Organic

Compounds ("VOC"s which are emitted from industrial, mobile and natural sources) can form ozone in the troposphere under certain meteorological conditions. The spatial and temporal effects of ozone formation is dependent upon the characteristics of the release, the composition of other pollutants in the atmosphere, and a variety of other factors. Photochemical modeling of NOx emission reductions from utility point sources in certain urban areas, for example, have demonstrated that an atmospheric scavenging effect can actually increase ambient levels of ozone downwind, under certain conditions, despite appreciable utility source NOx reductions. While a GPS will certainly impose additional costs upon the Delaware market, a state-imposed requirement will not insure that environmental disbenefits do not occur or that an economically-viable facility in another state operated under existing federal laws and requirements will not continue to operate to the benefit of customers in other markets where impediments do not exist. As a result, Delaware customers will be forced to pay above-market prices without receiving any commensurate environmental benefit.

Delmarva also opposes the adoption of NSPS for sources built prior to 1971. When the USEPA promulgated the NSPS concept two and one-half decades ago, it did so knowing that technological pollution control improvements on new facilities could be incorporated into the design of new facilities in a cost effective manner. The retrofitting of such controls on existing units is often impractical or cost prohibitive to justify. Older units would eventually shut down due to their age and would be replaced with newer units meeting lower emission standards. In addition, existing facilities that undergo "major modifications" that cause emission increases, would also be subject to applicable new source review requirements, including meeting the NSPS limits.

Delmarva believes that, from a national perspective, the existing environmental regulatory framework, combined with a market driven competitive electric services industry, will ensure that environmental progress continues to be made along these lines.

Delmarva believes that the independent development of a unilateral GPS for NOx in Delaware or the imposition of a NSPS requirement on older generating units is not sound environmental policy. The need for controls from all source types should reside with federal and state environmental regulatory agencies who can integrate the environmental aspects of the acid deposition control (SO_2 and NOx) provisions c Clean Air Act Amendments of 1990 with the ozone attainment activities (e.g. reg NOx controls with cap and trade programs) that are presently being discussed and implemented. For example, the Ozone Transport Assessment Group or "OTAG" (a coordinated 37 eastern state technical ozone modeling effort) is working closely with the USEPA to determine the need, location, and source categories that may need to undergo additional NOx controls in an attempt to alleviate the pervasive ambient ozone non-attainment problem. Imposition of unilaterally proposed GPS or NSPS retrofit requirements in Delaware would not incorporate the regional and national efforts that are presently underway by environmental regulators and would put Delaware at an economic disadvantage with other states. At the same time, they will impede the ability of competitive electric supply industry to generate more efficient mechanisms for addressing the same concerns in a market-oriented manner.

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June 30, 1997

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RE: P.S.C. Case No. 8738

Dear Mr. Gahagan:

Enclosed for filing with the Commission are the original and nineteen (19) copies of Delmarva's comments on Staff's Report, "A Framework for Customer Choice and the Future Regulation of Electric Services in Maryland", submitted May 30, 1997, as part of Case No. 8738.

In addition, the Company's comments are being submitted electronically as specified by the Commission's letter to Delmarva dated March 20, 1991.

Copies of this filing are being provided directly to the individuals indicated below.

Please acknowledge receipt of this filing by stamp receipting or signing the duplicate copy of this letter and returning it to me.

Very truly yours,

William R. Moore, Jr.

William R. Moore, Jr.

Enclosures

jrs/letter/amc

cc: Attached Service List

STATE OF MARYLAND
PUBLIC SERVICE COMMISSION

Case No. 8738 - Revised Service List
June 20, 1997

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DELMARVA POWER & LIGHT COMPANY'S COMMENTS REGARDING MARYLAND STAFF'S REPORT: MARYLAND PUBLIC SERVICE COMMISSION'S INQUIRY INTO THE PROVISION AND REGULATION OF ELECTRIC SERVICE

CASE NO. 8738

June 30, 1997

I. Introduction

Delmarva Power & Light Company ("Delmarva") files herewith its initial response to the MPSC Staff's report, "A Framework for Customer Choice and the Future Regulation of Electric Services in Maryland," dated May 30, 1997, in Case No. 8738. The purpose of this document is to provide the Maryland Public Service Commission ("the Commission") and its Staff with Delmarva's preliminary views on how the electricity industry should be restructured, and suggestions regarding Staff's proposed implementation framework.

While the report recommends allowing competition to set prices for electricity, the requirement that electricity also be sold by the incumbent utilities at a regulated price creates a fundamental flaw in Staff's proposed framework for restructuring. This combination of regulation and competition will distort the market for electricity and constrain the efficient use of utility generating assets, and create an uneven playing field for the emerging competitive market.

II. Delmarva's View of Restructuring

A. Delmarva's Four Basic Guidelines

As noted in its comments to this Commission two years ago in Case No. 8678, Delmarva believes that there are four basic guidelines that should direct the restructuring of the electric industry. The first principle is that regulation should be eliminated where competition exists. In the case of the generation market, competition is developing rapidly and thus the elimination of regulation is appropriate when customer choice begins.

Second, Delmarva believes in fair competition for all market participants. Utilities should be able to participate in competitive markets without being restricted, taxed, or otherwise burdened with requirements or costs that do not apply to other competitors. Pricing flexibility, maintaining confidentiality of sensitive customer information (in a way that does not create undue barriers to entry for competitors), and providing the opportunity to earn returns reflecting the increased risks of competitive markets are important for promoting fair competition.

The third principle is performance-based regulation. For those portions of the industry that remain regulated, performance-based regulation will provide flexibility in pricing, enabling the utility to meet special customer needs. This will not only enhance benefits to customers located in Maryland, but will also provide the utility with earnings opportunities based on good performance and improve efficiencies in the remaining regulated areas of the business, while helping to keep prices low.

Fourth and finally, full stranded cost recovery must be allowed. Delmarva agrees with Staff that utilities should have an opportunity to fully recover all prudently incurred, verifiable, and unmitigated stranded costs.

B. Delmarva's Collaborative and Forum

In late 1996, Delmarva developed and presented its own proposed framework, or "strawman" for restructuring, as part of the Delaware Collaborative and Maryland Informal Forum for Retail Competition. Key elements of the strawman included:

- A four year phase-in to choice, beginning with 10% of customers on 1/1/99, 20% on 1/1/00, 40% on 1/1/01, 70% on 1/1/02, and 100% on 1/1/03.
    - The same percentage of each customer class, in terms of energy/load, to be opened to competition at same time.
    - Customer selection to be determined by lottery. Customers must elect 100% of load by location.
    - For customers who did not/could not choose, Delmarva to continue to provide energy, at least through a transition period.
- Rates to be unbundled beginning 1/1/99.

- During the transition period, a generation price subdivided into 2 components: a retail market energy supply price (based on an estimate of market prices for 1999-2002) and a Competitive Transition Charge (CTC) to recover stranded costs.
    - Elimination of the fuel adjustment clause as of 12/31/98. Any remaining deferred fuel balance to be recovered or credited via a "correction factor" in 1999.
- For customers who have not yet obtained the option to choose another supplier, the total generation price (energy supply plus CTC) to be fixed at 1998 levels for 1999 through 2002. Prices for generation to be determined by the market beginning 1/1/03.
- Continued regulation of the distribution delivery charge under a Performance Based Ratemaking (PBR) plan beginning 1/1/99, subject to periodic Commission review.

- Stranded costs will be recovered from all customers via a non-bypassable CTC charge from 1999-2002 (with the exception of nuclear decommissioning costs, which will be recovered over the plants' remaining lives).

Delmarva believes that its proposals present a useful framework for consideration of competition in the electric industry.

III. Discussion of Staff's Recommendations

RECOMMENDATION 1:

All customers of Maryland investor-owned utilities will have the choice to enroll in Commission approved electric delivery service beginning no later than December 1, 2000 for service beginning April 2, 2001. At least one delivery service option will be available to 100% of all customers in all customer classes.

Delmarva believes that the time period and phase-in approach it proposed in its Informal Forum (outlined above) provides a more reasonable approach to implementing customer choice. A slightly longer implementation period will further mitigate stranded cost challenges, and the Company's proposed phase-in will allow for adjustments and refinements that will result in a smoother transition to customer choice.

A. Potential Benefits of Competition

No comment.

B. Electric Delivery Service

On page I-27, Staff notes that "Those customers who choose to purchase electricity directly from a generator, marketer, broker or other entity...will arrange for its transmission and distribution through the delivery services of the distribution utility." It is unlikely that customers will "arrange" for a delivery service option; instead, Delmarva envisions that the competitive supplier will coordinate the provision of transmission and distribution services with appropriate transmission service providers and distribution service providers, respectively. All similarly situated customers of a distribution utility should be provided comparable delivery services, irrespective of whether they are purchasing energy supply from the distribution utility or a competitive supplier.

C. Requirements for Electricity Suppliers

1. Operational Requirements must conform with PJM and APS reliability criteria

Staff states that planning for supply over the long term would be the responsibility of suppliers offering services to customers who choose direct access, and this would be a contractual matter between the customer and the supplier. Delmarva questions Staff's assumptions regarding long term supply planning beyond the term of the contract and the potential differentiation in treatment for distribution utilities and competitive suppliers. Delmarva would propose that supply obligations (long and short term) are most efficiently determined by market forces.

D. Utility Standards of Conduct

Delmarva agrees that Case No 8747 is the proper proceeding in which to establish appropriate standards of conduct.

RECOMMENDATION 2:

The proposed Regulatory Framework will apply only to investor owned utilities at this time. All other utilities may comply with this framework at their option. On May 1, 2000, Staff will make recommendations to the Commission regarding those non-investor owned utilities that remained under the prior regulatory structure.

A. Application to All Maryland Investor Owned Utilities

No comment.

B. Legal Issues Related to Restructuring Municipals and Cooperatives

No Comment.

C. Muni and Coop Option

Staff recommends that municipal and cooperative utilities have the option to refrain from full retail access prior to May, 2000. However, Staff's argument assumes that municipal and cooperative customers should not have access to the additional savings (estimates range from a nominal amount to 50% of current prices) arising from retail choice, a benefit that will accrue to the remaining 92% of Maryland's customers. Delmarva requests that the Commission adopt a provision whereby municipals and cooperatives (including any related affiliates, partners, or alliances) that are not participating in retail access for their own customers not be permitted to offer electricity supply service to customers of investor-owned utilities in Maryland.

RECOMMENDATION 3:

IOUs will put into effect for all customers unbundled rates approved by the Commission no later than April 1, 1998. All other utilities will put into effect for all customers unbundled rates approved by the Commission no later than September 1, 1998.

Delmarva recognizes that the Commission's Order for this proceeding stated that the unbundled rates which are to be reviewed in the roundtables "shall be revenue neutral with respect to customer class and, to the extent possible, revenue neutral for the bulk of individual customers within a customer class." (Order at 5). However, this position does not allow for the proper alignment of rate elements towards the cost of providing each service. In addition, unbundling rates, given the class revenue neutrality requirement, may lead to artificial market barriers, or, conversely, to a subsidization of some unbundled services by others. Delmarva acknowledges Staff's recognition that modifications may be required as rates are unbundled.

In addition, Staff's report gives little guidance on the issue of pricing of unbundled services. The report states that utility services will be unbundled along functional lines (i.e., generation, transmission, and distribution). In addition, there is some mention that there may be further unbundling of "behind" the meter services, such as billing and meter reading.

Delmarva believes that considerable care must be taken with respect to the pricing of unbundled services. The issue of unbundling services has been hotly contested in the telecommunications industry. Under the Telecommunications Act of 1996, local telephone utilities were required to unbundle their services and to offer access to long-distance carriers and to competitors offering local exchange service. The debate has centered on the pricing of access and other services. Not too surprising, the long-distance carriers have argued for the use of long-run incremental cost exclusively. However, long-run incremental cost methodology may not allow electric utilities to recover their joint and common costs.

Delmarva believes that a policy needs to be articulated which ensures that: (1) the incumbent utility recovers its joint and common costs, (2) unbundled services are priced as efficiently as possible, and (3) the pricing mechanism will reflect the nature of the competition facing each service.

RECOMMENDATION 4:

Customer retail access to competitive electric supplies will begin through prototype delivery service programs. Prototype programs will at a minimum have all the regulatory, administrative, operational and market structure characteristics of delivery service intended for all customers. Prototype programs will run for two years. Eligibility will be limited to 10% of each customer class' load in the first year and a total of 20% of each customer class' load in the second year. Suppliers and customers will agree to undertake or participate in whatever analysis, reporting, and operational requirements may be needed to evaluate and refine delivery service. Except for their limited enrollment, and possible special monitoring requirements, these prototype programs will comply with all other Recommendations.

Staff's time table for choice appears to be extremely ambitious. While Staff's recommended percentage of customer participation in the prototype program of 10% of load in the first year, and 20% in the second year seems reasonable, offering direct access to 100% of investor-owned utility customers by the year 2001 represents a jump of approximately 11,000,000 MWh (representing approximately 400,000 customers), to over 52,000,000 MWh (representing approximately 2 million customers) in one year (based on 1995 data). Delmarva is concerned that insufficient time is being allowed to: (1) agree on exactly how open access will be implemented, (2) educate customers, and (3) develop the systems required to implement open access. This is an extremely complex undertaking. States that have a substantial head start on Maryland are experiencing considerable difficulty in implementing open access. For example, with only six months remaining, California is still attempting to gain agreement on key implementation details. They still have not resolved something as fundamental as the appropriate method to be used to estimate the loads of customers that are too small to be billed on time-of-use meters. (The investor-owned utilities argue that these customers should be billed based on utility developed class average load profiles. Marketers argue that this approach will make it impossible for them to offer discounts to customers that are less costly to serve than the class average.) As noted in Section II above, Delmarva's strawman proposes a four year phase-in to customer choice.

RECOMMENDATION 5:

Enrollment in Commission approved prototype programs will begin December 1, 1998 for service beginning April 1, 1999. Enrollment will begin for the second prototype program year December 1, 1999 for service beginning April 1, 2000.

As noted in Section II of these comments, Delmarva's strawman requires that customers nominate 100% of load by location for customer choice.

RECOMMENDATION 6:

To speed the introduction of choice, the incumbent utility will continue as the provider of distribution related service for all existing customers during the first prototype program. Further unbundling will be considered at a later date.

A. Access to Distribution Service

Delmarva agrees with Staff's comments on page I-48 that the incumbent distribution utility "will continue to be authorized to provide distribution services within its service territory. It will continue to have the obligation to extend the network to provide service to all consumers." Delmarva notes that this will require modifications to revenue tests for Contributions in Aid of Construction for line extensions.

Also, Delmarva agrees with Staff that the incumbent distribution utility should continue as the provider of distribution-related services for all customers. As noted in Section II of these comments, Delmarva would propose the institution of a performance based ratemaking (PBR) plan for the regulated distribution business. A PBR improves upon traditional cost of service regulation in a number of ways. It allows the regulated utility more pricing flexibility, promotes cost efficiency, and generally decreases the extent of regulatory oversight. Delmarva believes that a PBR plan would be a valuable tool for the distribution business, and should be included in Staff's proposed framework.

RECOMMENDATION 7:

A regulated electric supply will be offered by the incumbent distribution utility to all customers. The Commission Staff will review and make recommendations as necessary on the regulated electric supply option on or before November 1, 2004.

In Recommendation 7, Staff requires the distribution utility to offer its customers a regulated supply option under both the prototype and full retail access programs. Staff details two regulated supply options: Option A is basically a modification of the current regulatory model, while Option B is a competitive bidding model under the monitoring and oversight of the Commission. Delmarva strongly opposes these proposals. Both options essentially call for the continued regulation of supply for those customers which do not/cannot exercise choice of generation supply resulting, in effect, in a divided marketplace.

The Staff is suggesting that the generation function of the electric power industry is no longer a natural monopoly, and that power suppliers can and should directly compete. Delmarva agrees with this assessment. Further, Delmarva firmly believes that a fully competitive marketplace for electric generation will result in the most efficient allocation of resources, thereby lowering prices to all consumers.

Staff's "Illustrative Regulated Supply Option" envisions that the incumbent distribution utility use its existing generation capacity to provide service to all customers that choose the regulated supply option. It is envisioned that the utility will be allowed to market any capacity that becomes available due to customers' choosing retail open access. Staff's report goes on to say that if the value of the released capacity is above the revenue requirements for the generation capacity, then there would possibly be a credit to customers' delivery service bills. Conversely, if the value of the released capacity is below the revenue requirements for the generation capacity, then delivery service customers might have a continuing responsibility for either all or part of the difference between the market value and the revenue requirements associated with the capacity, creating a "death spiral" where costs are spread over an ever-diminishing customer base. Moreover, in its "Guiding Principles" the Staff states the belief that no customer who chooses to purchase the regulated supply option will be made worse off.

In essence, Staff is proposing to deregulate all but the generation capacity required to provide the regulated supply option. This would result in a two-tiered generation market. One market would be competitive and the other regulated. The apparent reason for retaining the regulated supply option is to ensure that no customer will be worse off under open access than under cost-of service regulation.

Unfortunately, because of differences in the cost of serving customers (due to such factors as time-of-use, size, and load factor) and cross subsidies inherent in the current average cost based class rates, it is not efficient or desirable to guarantee that all customers will be better off under open access. Delmarva is concerned that Staff's attempt to pursue this objective will greatly reduce the potential benefits of open access, and could undermine the financial viability of incumbent utilities.

Delmarva believes that there are numerous defects in Staff's proposal. First, by eliminating generation capacity from the market, it hampers the development of a vibrant competitive market.[1] Second, it reduces the incentives for incumbent utilities to be efficient and to offer innovative products and services.[2] Third, it will lead to the formation of a two-tiered price system in which customers that benefit from obtaining generation services from the competitive market (generally customers whose cost to serve is low) will take this option, whereas customers that benefit from purchasing generation on the regulated tariff (generally customers whose cost to serve is high) will pursue this option.

The ultimate result is that the incumbent utility will be left with customers that are, on average, more costly to serve. However, since under Staff's proposal, the utility is restricted from increasing its rates above levels that exist at the onset of open access, it

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[1] A competitive market provides incentives for firms to be efficient in the generation of electricity (in the economic literature this is referred to as technical efficiency) and to introduce innovative products.

[2] This statement assumes that the regulated supply option will continue to be regulated under cost-of-service regulation.

will be difficult for the utility to recover those higher costs. It will be able to do so only if it is allowed to violate Staff's principle that no customer who chooses regulated supply be worse off. Moreover, some customers receiving the regulated supply option are likely to be paying a price that is less than the marginal cost to serve them. Charging a price that is less than the marginal cost to serve a customer is economically *inefficient*, and would result in resources not being directed to their highest valued use.

The outcomes discussed have parallels in other industries such as natural gas, telecommunications, and airlines. For example, in natural gas the existence of regulated, as opposed to market determined, prices led first to shortages in the 1970s followed by excess supplies in the 1980s. Also, the existence of a two-tiered price system consisting of strict controls on old gas (which kept prices below market levels) and relaxed controls on new gas caused the prices for new gas to climb above market-clearing levels as pipelines, in anticipation of future shortages, bid up prices.

Eventually pipelines with smaller old gas "cushions" faced higher average prices. This led to many contract disputes as customers attempted to obtain gas from lower cost supply sources and pipelines sought to avoid losses from take-or-pay obligations with producers. By the end of 1986, ten billion dollars worth of contracts were involved in take-or-pay disputes.[3] The situation was finally resolved when gas procurement (the gas equivalent of generation) was deregulated under FERC Orders 436 and 500, and larger customers and utilities on behalf of smaller core customers were able to obtain gas supplies at a single market-determined price.

Similarly, the initial plans for airline industry deregulation called for gradual deregulation. However, the tension created between the regulated and competitive sectors of the industry were sufficiently disruptive to compel the rapid conversion of the entire industry to competition. These same types of tension have led to the rapid reduction of regulation in the long-distance telephone market.

It is reasonable to require the incumbent utility to be the supplier of last resort. However, the price charged for this service should be the market clearing price (plus any

[3] Wald, M., *Gas Producers See and End to Disputes with Pipelines*, New York Times (November 7, 1988).

administrative cost required to offer this service) that will result if all generation units are allowed to compete. A robust competitive market is more likely to result if all the generation capacity of the incumbent utilities is deregulated or released to the market.

Such an approach has the following advantages. First, all customers will pay the market clearing price, which by definition is economically efficient.[4] Charging the economically efficient price will induce all customers to use resources efficiently. Second, it will promote vigorous competition, which will induce efficiency and the introduction of products that better meet customer needs.

In view of the foregoing, Delmarva respectfully requests the Commission to reject the recommendation of Staff to create a partial deregulation scenario for electric power generation.

RECOMMENDATION 8:

State tax law should be modified to preserve existing revenues to State, county, and local governments. The policy should not confer competitive advantages to particular market participants.

Delmarva agrees that differing tax burdens should not confer competitive advantage. Delmarva wishes to reiterate Staff's point that electric utilities are placed at a competitive disadvantage relative to other forms of suppliers due to the tax structure in Maryland (most notably in the case of property taxes). Delmarva agrees with Staff that tax reform is necessary in Maryland before the electric industry is restructured.

RECOMMENDATION 9:

The Commission should proceed with a comprehensive review of the Public Service Commission law to identify statutory provisions which need to be modified to facilitate customer choice. Changes in the law should allow the Commission maximum flexibility to address the issues which will arise in connection with implementing a new regulatory framework.

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[4] Efficiency in this context means that the generation service is priced such that society's resources are put to their most highly valued use. In the economic literature this is usually referred to as allocative efficiency.

To preserve a level playing field in a competitive environment, the definition of an "electric company" in Article 78 § 2(f) should be expanded to include marketers, brokers, and all other entities dealing directly with Maryland electricity customers. Customers of these entities should be able to file complaints with the Commission concerning charges and services. The Commission should have oversight over the Maryland activities of all such entities, who should be approved by the Commission prior to commencement of service, have a Maryland presence, file annual reports with the Commission and be subject to other appropriate Maryland regulatory requirements, consistent with their level of activity in Maryland.

The rate-making provisions of Maryland law should be revised to facilitate competition, and to address transitional provisions required for the prototype programs recommended by Staff. Once competition is in place, the law should provide for the incumbent the same degree of pricing flexibility available in Maryland to all authorized competitors of the incumbent.

Maryland tax laws should be reviewed and revised, where appropriate, to protect against any unfair tax burden that may be imposed upon the incumbent but not on competition.

A general review of Article 78 and COMAR regulations implementing the Public Service Commission Law should be conducted, again with a view to make sure that a level playing field is created for the new competitive environment.

RECOMMENDATION 10:

Appropriate customer information and safeguards should accompany the introduction of retail access. The Commission should seek legislative guidance on whether Maryland should establish an economic assistance program funded by a universal access charge or rely on existing and expanded state programs.

Delmarva agrees that specific customer protection policies should be established as the industry is restructured. Delmarva also agrees that the distribution company should not deny or disconnect service based upon a customer's payment problems with a third-party supplier. However, the distribution company should not be obligated to provide these customers with a regulated supply option (as previously discussed). Customers and suppliers involved in billing disputes should have the opportunity to seek restitution through the proposed dispute resolution process, and those customers should have the option to seek service from another third-party supplier. The existing Maryland program for customers with financial difficulties should be continued on an unbundled basis, and expanded if necessary. However, it is premature to assume that these customers should automatically be returned to a regulated supply option, which may offer supply prices which are even more uneconomical to the very consumers who can least afford to pay. In addition, these customers may ultimately be attractive from a marketing perspective to a number of competitive suppliers.

An alternative to Staff's regulated supply option would be to establish a "risk pool" of certain customers, who would then be distributed to all suppliers serving Maryland, on a proportionate basis. This would result in a sharing of "high risk" customers among all suppliers.

RECOMMENDATION 11:

To contribute to the preservation of environmental quality, the Commission should maintain jurisdiction over the siting of power plants in Maryland.

The regulations governing certificate requirements should be revised so that no entity seeking to construct a generating facility has an unfair advantage over other suppliers.

RECOMMENDATION 12:

Electric supply reliability should be maintained by reliance on an installed capacity obligation. Development and enforcement of this obligation will be the role of an ISO.

No comment.

RECOMMENDATION 13:

Utilities should have the opportunity to recover prudently incurred, identifiable, and unmitigated stranded costs. Ratepayers should have the opportunity to benefit from all assets acquired under regulation.

Delmarva agrees with Staff that utilities should have the opportunity to fully recover stranded costs. Delmarva would, however, like to clarify some issues regarding the calculation and recovery of stranded costs. Comments on Paragraphs C1, D and F of Recommendation 13 are set forth below.

C.1. Determining Stranded Costs

Focusing on market based valuations (versus non-market based valuations) - stranded costs should be determined using the calculated value of **net** stranded assets in a competitive environment, versus their value under regulation. Stranded costs can be calculated as a function of the expected future market price of the assets versus their adjusted book value (net book value plus or minus deferred taxes and investment tax credits). Delmarva agrees with Staff that an administrative determination of the market value of net assets is uncertain, compared with an outright sale of generating assets. However, the administrative method avoids many pitfalls associated with a divestiture. These include transaction costs associated with liquidation and the potential to depress the price of assets, if a significant amount were to be placed on the market at the same time.

D. Recovery of Stranded Costs

The net amount of each utility's stranded costs should be recovered via a non-bypassable transition "wires" charge (in place of an exit fee) that would be paid by all customers. If the net amount of stranded costs is negative (i.e., the utility has a stranded benefit associated with releasing assets for competition, using a market-based valuation approach), this amount should be returned to consumers, via a transition "wires" credit. Delmarva believes that this charge or credit represents the opportunity for generators to compete and customers to benefit from competition in the generation market.

Transition charges will most likely be minimal in Maryland, given the relatively low level of stranded costs anticipated to be incurred by Maryland utilities, compared with those in other states. It should be noted that consumers will not truly be made worse off during the transition period if the total price for generation plus the transition charge is not greater than what it would have been under continued regulation.

F. Nuclear Decommissioning

Delmarva agrees with Staff's assessment that the continued funding of nuclear plant decommissioning trust funds is vital to the public health and safety, and that these costs must be recovered over the respective plant lives.

RECOMMENDATION 14:

Retail market power will be considered as part of each utility's overall retail access program.

With barriers to retail competition lowered, (i.e., opening retail markets as contemplated in Maryland and surrounding states, as well as providing open access to the transmission systems for generators throughout PJM), it may not be necessary to consider market power as part of each utility's overall retail access program, as Staff recommends. The incumbent distribution utility has a 100% market share of its Commission-designated service territory irrespective of who generates the electricity or provides the transmission services necessary to transmit the electricity from the generator to the distribution systems.

The Commission's analysis of retail market power should start with defining the relevant market, which is unlikely to be substantially different than the relevant market for wholesale market power. However, there are likely to be substantial differences in terms of market participants. Incumbent distribution utilities are only the starting point from a historical perspective. New participants are already appearing even though markets have not yet opened. Some current participants may also leave the market. For example, some generators may choose to sell only at the wholesale level.

Delmarva also has some concerns regarding Staff's reference to market power being "calculated as market share." This statement is much too simplistic a definition of market power, because it fails to consider the profitability of a supplier's behavior or the period over which a supplier is able to influence market prices. For example, a supplier could reduce its price and thus trigger a reduction in overall market prices; however, this is not market power. Second, a supplier with a relatively large market share could withhold output and by so doing increase the market price. However, if this higher market price induced others to enter the market within a relatively short period, then the additional capacity offered by these suppliers could reduce market prices to their previous levels. In this example, the increase in market prices is short-lived and does not demonstrate market power. These factors should be taken into consideration before the Commission rules on the necessity of market power studies for this proceeding.

RECOMMENDATION 15:

Utility specific Roundtable processes organized by the Commission Staff will be the primary vehicle for the implementation of these recommendations. The Roundtable process will attempt to produce supported utility findings to implement this Framework. Staff will report to the Commission at least every three months beginning September 1, 1997 on those issues that in its opinion do not appear resolvable in the Roundtable process. For those issues, Staff will propose alternative procedural recommendations that address the required restructuring deadlines.

Delmarva has some concerns regarding the use of a roundtable process to address many of the issues set forth in Staff's report. In general, Delmarva believes that a roundtable as part of a collaborative effort to gain understanding and reach consensus on issues is advantageous. Indeed, Delmarva has used the collaborative approach to establish its own restructuring proceedings in Delaware and Maryland. In this situation, however, care must be taken to ensure that the process results in a timely transition to competition and that major restructuring policies are ultimately established by the Commission as an integrated package.

IV. Conclusion

In conclusion, Delmarva agrees with most of the principles and certain portions of the Recommendations set forth by Staff in its report. Delmarva would suggest that one of the critical themes of any restructuring effort in Maryland should be that competition is beneficial, desirable, and will lead to economic development in the state. As such, regulators should focus on major policy issues, and move away from the mind-set that competition needs to be "managed." Delmarva looks forward to addressing these issues further as Case No. 8738 progresses.

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VIA AIRBORNE EXPRESS

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**RE: Commission's Inquiry Into Electric Industry Restructuring
Case No. 8738, Delmarva's Supplemental Comments**

Dear Mr. Gahagan:

Enclosed for filing with the Commission are the original and nineteen (19) copies of Delmarva's supplemental comments for the Commission's consideration in Case No. 8738

In addition, the Company's comments are being submitted electronically.

Copies of this filing are being provided directly to the individuals indicated below.

Very truly yours,

Peter F. Clark

Peter F. Clark

DOCKETED
OCT 22 1997

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Case No. 8738 - Revised Service List
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In the Matter of the Commission's Inquiry into the Provisions and Regulation of Electric Service. * * *

Case No. 8738

Supplemental Comments of Delmarva Power & Light Company

** *** **

Regulated Supply Option

As Dr. John Landon discussed in both his prepared statement and in his testimony before the Commission, Staff's proposed regulated supply option suffers from five principal defects. Moreover, an alternative exists which is preferable to Staff's proposal. Dr. Landon made the following points:

- First, the regulated supply option will reduce the scope of the competition by eliminating generation assets from the marketplace. This, in turn, will reduce incentives for suppliers to operate efficiently and to be innovative.

- Second, the dual market structure (regulated and unregulated) will lead to adverse selection in which high-cost customers will choose the regulated supply option while low-cost customers will choose to purchase from the competitive market. This will make it impossible to freeze rates for the regulated supply option, as Staff is proposing.

- Third, because customers choosing the regulated supply option will be paying less than the marginal cost of service, resources will not be allocated to their highest-valued use.

- Fourth, the regulated supply option is expected to increase stranded costs compared to releasing the generation assets to the competitive market.

- Fifth and finally, experience in other industries (including natural gas, telecommunications, airlines, and trucking) has shown that attempts to offer consumers a choice between regulated and competitive options leads to unsustainable outcomes, eventually culminating in the complete deregulation of the market.

Staff continues to advocate the implementation of a regulated supply option as a means of ensuring that no customer is made worse off as a result of deregulation. However, because of differences in the cost of serving customers (due to such factors as time-of-use, size, and load factor) and cross-subsidies inherent in the current average cost-based class rates, it is neither efficient nor desirable to guarantee that all customers will be better off under open access. It is also unfair to require the incumbent utility to provide this guarantee without adequate compensation. In a competitive generation market, the prices consumers pay for electricity will reflect the true cost of serving them. As a result, high-cost consumers may pay more and low-cost customers may pay less for electricity than they currently do under traditional cost-of-service (COS) regulation.[1] However, in the long term, it is anticipated that competition between generation companies is likely to drive prices down to a point where all consumers are better off under open access than they would otherwise be under traditional cost of service regulation. Staff has not presented any convincing rationale for continuing to regulate existing generators while opening their markets to competition. Staff takes the view that competition among existing generators doesn't count, as indicated in Mr. Timmerman's comments. Staff appears to be preoccupied with the ownership or control of existing generation within the PJM area and import capability. Mr. Timmerman's testimony hypothesizes that competitive pressures may result in regulated energy offerings that are in fact competitive and desirable for customers, however, neither Staff nor any other party can provide examples from other industries to support his proposition.

Delmarva agrees with Staff that the incumbent utility should be the supplier of last resort. However, Delmarva believes that the price for this service should be the market clearing price (plus any administrative cost required to offer this service), not a regulated price.

[1] Under COS regulation, both low- and high-cost customers pay a single average rate in which low-cost customers subsidize high-cost customers.

Finally, if policy makers believe it is necessary to subsidize some customers to ensure that their costs will not increase under open access, this could be done by using whatever method the Commission chooses to fund other social programs (*e.g.*, promoting the efficient use of energy or providing assistance to low-income customers). However, to avoid distorting the price signals, Delmarva believes that such societal programs should be funded through an access charge, or some similar mechanism which does not distort price signals, which would be assessed at the distribution level, and that the total charge must be small.

Unbundled Metering and Billing

Staff has recently changed its position on the treatment of metering and billing services in a competitive retail environment. Staff witness Timmerman stated in his testimony that "Staff now recommends that... all electric suppliers should have the option of installing their own meters and rendering their own bills to end users for their services." Delmarva's position on billing is that consumers should have the choice between three options:

(1) Separate Local Distribution and Energy Supply bills;
(2) Local Distribution and Energy Supply charges aggregated on one bill from the local utility; and
(3) Local Distribution and Energy Supply charges aggregated on one bill from the supplier.

With respect to Staff's metering proposal, Delmarva opposes allowing deregulation of metering at this time. Delmarva believes that attempting to unbundle the metering services will impose additional costs on consumers and could jeopardize restructuring. Once retail access has been successfully implemented, the Commission may wish to review the benefits and costs of unbundled metering. However, when deciding whether or not to deregulate metering, Delmarva believes that the Commission must weigh the benefits of increased competition with the following negative consequences:

1) Experience strongly suggests that coordination problems in a competitive market for metering will lead to significant disruptions and could compromise system reliability, safety and quality of service;
2) Loss of economies of scale in the acquisition of metering equipment;
3) Loss of economies of scale or density in the installation of meters;
4) Loss of economies of scale or network externalities in the collection of electricity consumption data;
5) Loss of economies of scope between metering and distribution services;
6) Loss of regulatory economies of scale in the oversight of metering including control of accuracy and calibration records;
7) The competitive provisioning of metering would likely increase stranded costs and complicate the recovery of stranded costs associated with generation assets;
8) Commission oversight will increase in complexity; and

9) A competitive marketplace may not be able to deliver the socially optimal deployment of advanced metering. Advanced metering is expected to generate significant social benefits.

While all of the above negative consequences are important, Delmarva offers additional comments on coordination problems, economies of scale and scope and stranded costs.

Coordination Problems

There are expected to be many coordination problems associated with unbundled metering. If independent firms are not properly integrated with generation services, there may be serious coordination problems in the implementation of new metering systems. Accurate and efficient billing can occur only if metering information is provided on time, free of errors, and in usable form. If many different metering companies must send information to many different billing companies, the possibility of delays and errors increases. Furthermore, coordination problems in the competitive provision of metering could lead to significant problems with settlement, load imbalances, and other serious issues that might affect both the settlement process and system reliability.

The experience in the United Kingdom proves this point. The United Kingdom implemented retail access in 1994 with competition in the provision of metering services. However, the U.K. has experienced significant coordination problems as a result. Customers who had contracted for advanced metering systems did not always receive them in a timely fashion, and many of the new meters that were installed were not properly connected to the data collection network. In the first six months, usage for over 50 percent of the customers that had signed up for new metering systems was not properly recorded. As a result, bills for these customers had to be estimated. There were problems with load imbalances and the distribution companies' cash flows suffered considerably.[2]

[2] Henney, Alex, "Competition, Confusion, and Chaos: The Metering Muddle," Public Utilities Fortnightly, 134:20 (November 1, 1996), pp. 26-29.

Safety is another concern that the Commission must consider. Delmarva has strict standards regarding meter quality and installation. Open competition could pave the way for inferior "offbrand" metering equipment being installed by poorly trained technicians. An inferior meter and/or installation could put the residence and part of the distribution system in jeopardy. Obtaining access to a meter not owned by the utility could also pose additional problems for the local utility during emergencies.

Economies of Scale and Scope

As the sole provider of meters, the local utility can realize greater economies by purchasing on behalf of all customers than could several service providers. Once the utility has obtained the meters, it can then exploit the economies of scale or density in the installation of meters in a given geographic area. Having a single firm install and read meters in every home in a neighborhood will require fewer resources than having several firms install and read the meters. As an example of the economies of density, consider on-site meter reading. A meter reader who reads every meter in a consecutive path will read 10 times more meters than one who reads every 20th meter.[3]

The traditional method of data collection, on-site meter reading, requires large investments in personnel and fleet services. Advanced methods being tested today are expected to lower the cost of data collection significantly. The advanced methods require connecting the meters on the customer's premises to the central data processing unit by a data communications network. While the choice of network – e.g., wireless or wireline – will influence the cost of service, the fixed costs remain large. However, once the network is brought to a neighborhood, the cost of serving additional customers in the area is very small. In other words, the marginal cost of service is less than the average cost, and adding additional customers to the network will lower the average cost of service to all customers.

The California proceedings provide compelling evidence of the dramatic economies of scale from widespread implementation of advanced metering. Estimates of the cost of providing metering service to small California customers in a multi-firm market vary widely—from a high of $27 per meter per month, to a low of $5 per month—based on assumptions of between 5 and 10 percent penetration.[4] On the other hand, Cellnet Data Systems, a leading provider of advanced metering technologies, has estimated that a

[3] King, Chris S., "Competition at the Meter: Lessons from the U.K.", Public Utilities Fortnightly, 134:20 (November 1, 1996), pp. 22-25.

[4] These figures represent total cost of service, including network infrastructure costs, meter acquisition and financing, and data collection costs.

saturated deployment of advanced metering would cost as little as $1 per meter per month for small customers. Thus, the minimum cost savings from exploiting economies of scale would be 5 times and the maximum might be as high as 27 times.

Stranded Costs

Allowing competitive firms to provide metering would substantially complicate stranded cost recovery. With competitive providers of metering, the Commission will need to revisit the issue of stranded cost recovery (in the context of metering). The cost of existing metering no longer being used for billing will need to be recovered. Moreover, to the extent that customers opt for other metering providers, the utility's average cost of providing metering is likely to increase relative due to lost economies of scale and scope.

Load Control

Staff questions whether load control programs should continue in a competitive retail environment, and, if so, which entity should be responsible for operating the programs and paying billing credits. The answer is simple; to the extent such programs provide a benefit, they will continue. Utilities will likely be willing to contract with energy suppliers to operate existing programs, or perhaps energy suppliers will develop their own programs. In any event, it is the energy supplier who should provide the billing credits, because it is their costs that will be avoided as a result of the program. Such programs provide no significant benefit to Transmission & Distribution systems.