

BEFORE THE PUBLIC SERVICE COMMISSION

OF THE STATE OF DELAWARE

IN THE MATTER OF THE APPLICATION OF)

DELMARVA POWER & LIGHT COMPANY FOR A)

CHANGE IN COGENERATION AND SMALL) PSC DOCKET NO. 99-674

POWER PRODUCTION RATES)

(FILED DECEMBER 30, 1999))

ORDER NO. 5497

This 11th day of July, 2000, the Commission finds, determines, and Orders the following:

I. BACKGROUND

1. Under Section 210 of The Public Utility Regulatory Policies Act of 1978, an electric utility, such as Delmarva Power & Light Company ("DP&L" or "the Company"), is obligated to interconnect with and purchase electric supply generated by qualifying cogeneration and small power production facilities ("QFs"). 16 U.S.C. § 824a-3(a); 18 C.F.R. Part 292. Unless agreed otherwise, the price that DP&L must pay for such QF-generated power is determined by looking to the Company's "incremental" or "fully-avoided" energy and capacity costs. 16 U.S.C. § 824a-3(b), (d); 18 C.F.R. §§ 292.101 (b)(6), 292.304(a), (b). Federal implementing regulations require state utility commissions, like this one, to put into effect standard rates for purchases from QFs with design capacities of 1000 kW or less. 18 C.F.R. § 292.304(c). Historically, this Commission has required DP&L to tariff, under Service Classification "X" in the Company's Electric Tariff, standardized rates for energy and capacity purchases made from QFs with a design capacity of 1000 kW or less. The Commission initially reviewed, and adjusted, such Service Classification "X" rates (including attendant metering and administrative charges) each year. However, in 1997, the Commission shifted its review to a biennial cycle, with the Service Classification "X" rates scrutinized as part of the Company's fuel adjustment clause docket for that year.

2. On December 30, 1999, DP&L filed an application to change its Service Classification "X" rates, both in terms of its actual rates as well as the underlying methodology used to calculate the prices and charges. Initially, DP&L proposes to continue to file for adjustments to its Service Classification "X" rates on a biennial basis. In addition, the Company proposes, supported by the pre-filed testimony of James R. Diefenderfer, to alter the methodology it uses to calculate its energy and capacity "avoided costs" which, in turn, underlie the Service Classification "X" rates. The new methodology would calculate both energy and capacity "avoided costs" -

and, hence, the Service Classification "X" rates - based on the offer prices for energy and capacity tendered in the emerging broker market for electric supply in the PJM region.

3. In PSC Order No. 5356 (Feb. 28, 2000), the Commission allowed DP&L's adjustments to its Service Classification "X" rates to go into effect, on a temporary basis. The Commission directed the Company to provide notice of these proposed rate adjustments to every QF which had, in the last five years, provided supply to the utility under the Service Classification "X" provisions. DP&L did so. Exh. 1. No QF filed comments nor sought intervention in this matter.

4. As announced in the earlier notice and in Order No. 5356, the Commission held a hearing on DP&L's application during its regularly scheduled meeting on May 23, 2000. There, DP&L presented Mr. Von Steuben and Mr. Diefenderfer, who each adopted his pre-filed direct testimony (Exh. 2). The Commission Staff, through the testimony and memorandum (Exh. 3) of Richard A. Latourette, Public Utilities Analyst, recommended approval of the proposed changes in the Service Classification "X" rates and the switch to a market-based methodology for calculating "avoided costs" in this context. Tr. 15-16. The Public Advocate also participated. She also supported the application (Tr. 14) but also endorsed, by memorandum (Exh. 7), changes to Tariff Leaf No. 27 of Section XI of the Company's Electric Tariff (Exh. 6). Those amendments, submitted by DP&L on May 15, 2000, would clarify that a supplier with less than one megawatt capacity - even if it did not meet the criteria for a QF or a "renewable-energy/net metering" customer - could still interconnect with DP&L's network so long as it fulfills the Company's technical guidelines for interconnection (including required approvals). Staff, by the memorandum of Rajnish Barua (Exh. 4), also supported this tariff alteration, noting that the changes would allow greater flexibility for customers and, thus, serve the public interest.

5. After considering the application and the written and oral testimony of the witnesses, the Commission approves the proposed rate alterations for Service Classification "X" as set forth in the December 30, 1999 application. The Commission also approves the amendments to Tariff Leaf No. 27 to Section XI of DP&L's Electric Tariff, as proposed in the revised tariff leaf filed on May 15, 2000.

II. FINDINGS AND DETERMINATION

"Avoided Cost" Methodology and the

Service Classification "X" Rates

6. As noted above, DP&L, in its application, seeks endorsement of a new methodology for calculating its "avoided costs" which, in turn, determine its Service Classification "X" rates for purchases of energy and capacity from QFs with less than 1000 kW capacity. As explained in detail in Mr. Diefenderfer's pre-filed testimony, DP&L proposes to change the "avoided cost" methodology from the present one - which uses costing capacity and energy costs - to one which looks to the supply market's forecast for capacity and energy prices. According to the Company, this shift in methodology: (a) would be consistent with the Company's decisions to transfer a large part of its generating assets to other independent producers or an affiliated, but non-regulated, generation

company; (b) would recognize the emergence of a market for energy and capacity sales within the PJM region; and (c) would produce Service Classification "X" energy and capacity rates which can be easily determined, verified, and updated.

7. Using this new methodology, the Company calculated the energy component of the Service Classification "X" rates by first developing a multitude of hourly market prices for the year 2000 and then, by use of a weighted averaging process, arriving at specific energy costs for on- and off- peak periods for both the summer and winter months. On the capacity side, the Company translated the market's offer price for capacity into a capacity rate to be paid monthly to suppliers under a monthly allocation factor. In contrast to present practice, where a Service Classification "X" QF is locked onto a fixed capacity payment for the term of its agreement, the new methodology permits capacity payments to be updated biennially based on the most recent view of the market.

8. Based on: (a) the absence of any objection from QFs providing supply under the Service Classification "X" standardized rates; and (b) Staff's recommendation, the Commission endorses DP&L's change in the methodology for calculating its "avoided costs" for determining Service Classification "X" rates. The Commission also approves the particular Service Classification "X" rates proposed by the Company using this new methodology. Finally, the Commission accepts DP&L's proposal to make adjustments to these rates on a biennial basis so as to allow for changes in light of changed market conditions.

9. The Commission also approves the revised Tariff Leaf No. 27 to Section XI that the Company submitted in this docket. Enabling all forms of relatively small, customer-owned or distributed generation to be interconnected with the Company's network (provided the generator can meet all technical standards) seems consistent with the policy of deregulation of supply mandated by the Electric Restructuring Act of 1999. As the Public Advocate reports, increasing the use of customer-owned distribution (of all kinds) may: (a) provide diversity in generation resources; (b) increase the reliability and efficiency of the grid and delivery network; (c) alleviate constraints related to load pockets and market dominance; and (d) provide customers with greater choice of supply. Indeed, the Commission understands that the changes to Tariff Leaf No. 27 result from agreements reached in DP&L's restructuring docket, PSC Docket No. 99-163.

10. Finally, the Commission endorses the Company's proposal calling for biennial review of the rates in Service Classification "X."

NOW, THEREFORE, IT IS ORDERED:

1. That the amendments and changes to the Service Classification "X" section of P.S.C. Del. No. 8 - Electric Tariff, as proposed in the application filed by Delmarva Power & Light Company on December 30, 1999, are hereby approved. This approval includes the changes in the "Energy Purchase Rates," "Capacity Payment Rate," "Monthly Customer Charge," and "Monthly Metering Rates," as set forth in the revised tariff sheets filed with the application. As set forth in the body of this Order, the Commission reserves the right to revisit the "avoided cost" methodology utilized to calculate the rates herein approved in a later Service

Classification "X" rate filing or in the context of determining or reviewing the appropriate rate to be paid for generation supply to a Qualifying Facility supplier having a capacity greater than 1000 kW.

2. That Delmarva Power & Light Company shall, beginning on December 31, 2001, file on a biennial basis, an application for adjustments to its Service Classification "X" rates.

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

BY ORDER OF THE COMMISSION:

/s/ Robert J. McMahon

Chairman

/s/ Joshua M. Twilley Vice Chairman

PSC Docket No. 99-674, Order No. 5497 Cont'd.

/s/ Arnetta McRae

Commissioner

/s/ Donald J. Puglisi

Commissioner

/s/ John R. McClelland

Commissioner

ATTEST:

/s/ Karen J. Nickerson

Secretary

