Delmarva Power & Light Company, Delaware

SUMMARY OF

Proposal to Energy Efficiency Advisory Council for
Energy Efficiency Rate Calculation and Recovery Procedure for Regulated Utilities

A. INTRODUCTION

Pursuant to the 2014 amendments to the Delaware Energy Act (the "EE Amendments"), Energy Efficiency Working Group (EEAC) members have been involved in the EEAC process. The statutory responsibilities of the EEAC include developing energy efficiency (EE) program portfolios for all utilities in Delaware. With respect to regulated utilities, the EEAC's additional statutory responsibilities include development of recommended rate recovery mechanisms. The EEAC must then recommend adoption of the programs and recovery mechanisms to the Commission for its review and approval. Delmarva Power has provided the EEAC with a more thorough document covering Delmarva Power's proposals for:

1. The recovery mechanism the EEAC should recommend to the Commission;
2. The procedure the EEAC should recommend to the Commission for the Commission's review and approval of:
   a. EEAC recommendations concerning EE programs and a recovery mechanism, and
   b. Annual EE Rate adjustments.
3. The manner in which the EE Rate should appear on Delmarva Power's bills.

This document is designed to provide a less technical summary of the proposals listed above. The more thorough document is provided as an attachment hereto.

B. EE AMENDMENT STATUTORY PROVISIONS RELATED TO RECOVERY

The following are the primary statutory provisions that the EEAC must keep in mind when considering the proposal summarized in this document:

1. The Recovery Process Must be Efficient and Timely
2. Costs May not be Placed in Rate Base

3. Rates Must be Annually Adjusted

4. The Rate Must Include Both Recovery of Costs and a Rate of Return

5. Commission Approval of Both EE Programs and Recovery Mechanism is Required

C. RATE COMPUTATION FOR DELMARVA POWER EE PROGRAMS

The rate computation mechanism proposed and summarized below for adoption in Delaware is based upon the mechanism proven to be efficient and effective in Maryland.

1. EE Rate Based upon Program Budget for Year-Ahead: The recommended first year of the EE Rate for regulated utilities will be established based upon the budget established by the regulated utility and the EEAC for the first year of the program.

2. Amortization Period of Five Years: Delmarva Power recommends a general amortization period of five years for EE programs.

3. EE Rate and Annual Amount Recovered – Year 1: The EE Rate is determined by calculating the annual amount to be recovered and dividing that amount by the forecasted KWh load. The annual amount to be recovered would consist of:

   a. Forecasted program costs;

   b. Forecasted amortization of program costs; and

   c. Forecasted rate of return on the unamortized balance.

4. Annual EE Rate Adjustments - Subsequent to Year 1: Subsequent to Year 1, the EE Rate will include the components outlined in Section C.3. above, to be annually adjusted as follows:

   a. Add forecasted amortized costs related to any additional EE programs recommended by the EEAC and approved by the Commission; and

   b. Adjust for prior period true-ups.

D. PROCEDURE FOR COMMISSION APPROVAL OF EEAC RECOMMENDED PROGRAMS AND RATE RECOVERY MECHANISM

Once the EEAC recommends both EE programs and rate recovery mechanisms for regulated utilities, those recommendations must be reviewed and approved by the Commission before implementation. Two types of Commission proceedings will be needed.

1. Recommended Commission Procedure for Approving
   EEAC-Recommended EE Programs and Recovery Mechanism

   Delmarva will file an Application for Approval of the EEAC recommendations. Delmarva anticipates that the Application will be supported by pre-filed testimony of at least three witnesses. It is anticipated that a rather traditional schedule for an evidentiary hearing will be established and followed.

2. Recommended Commission Procedure for Annual EE Rate Adjustments

   Because the EE Amendments provide that the Commission must utilize a recovery process that provides for annual adjustments to the EE Rate of the same type used for "other supply resources," Delmarva Power recommends the following annual process, which is similar to that used for annually adjusting Delmarva's Standard Offer Service ("SOS") rate:

   a. At least 60 days before new annually adjusted EE Rates are scheduled to go into effect, Delmarva will file an annual application for approval of an adjusted EE Rate for the upcoming 12 month period.

   b. At a regularly scheduled Commission meeting within a few weeks after the application is filed, the Commission will issue an order that: (1) opens a docket, and (2) permits EE Rates, as filed, to go into effect subject to refund within 60 days.

   c. Staff and DPA will conduct an audit of the annual EE Rate filing. In the event that Staff or DPA discover any errors during the audit process, EE Rates will be adjusted for the remainder of the annual period to account for the error.

   d. At the conclusion of the audit, Staff will provide a report to the Commission and at a regularly scheduled Commission meeting, the Commission will hear testimony and issue its final ruling on Delmarva's annual EE Rate adjustment.

The EE Rate and total monthly EE charge will be identified as a separate line item on bills of regulated utilities, rather than being bundled as part of other rates.

-END OF SUMMARY-

Attachment Cover Sheet

Delmarva Power & Light Company, Delaware

Proposal to Energy Efficiency Advisory Council for
<u>Energy Efficiency Rate Calculation and Recovery Procedure for Regulated Utilities</u>

A. INTRODUCTION

Pursuant to the 2014 amendments to the Delaware Energy Act (the "EE Amendments"), Delmarva Power, the Department of Natural Resources and Environmental Control (DNREC), and additional participants in a diverse group of appointed Energy Efficiency Working Group (EEAC) members have been involved in the EEAC process. The statutory responsibilities of the EEAC include developing energy efficiency (EE) program portfolios for all utilities in Delaware.[1] With respect to regulated utilities, which include Delmarva Power & Light Company and Chesapeake Utilities, the EEAC's statutory additional responsibilities include development of recommended rate recovery mechanisms.[2] The EEAC must then recommend adoption of the programs and recovery mechanisms to the Commission for its review and approval.[3] This document summarizes Delmarva Power's proposals to the EEAC concerning the following:

1. The recovery mechanism the EEAC should recommend to the Commission;

2. The procedure the EEAC should recommend to the Commission for the Commission's review and approval of:

    a. EEAC recommendations concerning EE programs and a recovery mechanism, and

    b. Annual EE Rate adjustments.

3. The manner in which the EE Rate should appear on Delmarva Power's bills.

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[1] 29 *Del.C.* § 8059 (h) (1) c. Provides: … "the advisory council shall review energy efficiency, peak demand reduction, and fuel switching *<u>program plans</u>* for each affected energy provider and *<u>recommend them for approval</u>* by the appropriate regulatory authority…."

[2] 29 *Del.C.* § 8059 (h) (1) e. provides: "Recovery of appropriate costs shall be through a *<u>rate-recovery mechanism</u>* that is consistent with the goals and objectives of this section and *<u>recommended by the advisory council</u>*, filed by the affected energy providers, and *<u>approved by the Commission</u>*."

[3] *See* footnotes 1 and 2.

B. EE AMENDMENT STATUTORY PROVISIONS RELATED TO RECOVERY

The EE Amendments contain several provisions that deal specifically with the recovery mechanism to be used by regulated utilities. The following are the primary provisions that the EEAC must keep in mind for purposes of considering the proposal outlined in this document:

1. The Recovery Process Must be Efficient and Timely: The recovery process recommended by the EEAC and ultimately adopted by the Commission must be both efficient and timely.[4]

2. Costs May not be Placed in Rate Base: EE Program costs may not be placed in rate base.[5]

3. Annually Adjusted Rate: The energy efficiency rate (EE Rate) shall be adjusted on an annual basis.[6]

4. Deferred Accounting: Regulated utilities are entitled to deferred accounting for the costs incurred in the development and implementation of EE programs.[7]

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[4] 29 *Del.C.* § 8059 (h) (1) e provides, in pertinent part:

> "Notwithstanding any provision in Title 26, the Commission shall approve the recovery of appropriate costs incurred by Commission-regulated affected energy providers for approved programs and portfolios *on an annual basis*, in the same manner as other supply resources, including allocated costs pursuant to this paragraph (h)(1).
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> ***
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> .... [T]he Commission shall utilize a process that achieves the *efficient and timely recovery on an annual basis* by commission-regulated affected energy providers...."

29 *Del.C.* § 8059 (h) (1) e 1 provides, in pertinent part:

> "...the Commission shall utilize a process that achieves the efficient and timely recovery ... by commission-regulated affected energy providers of appropriate *costs and associated rates of return* related to implementing activities and programs recommended by the advisory council."

[5] 29 *Del.C.* § 8059 (h) (1) e 2.

[6] See, footnote 4.

[7] 29 *Del.C.* § 8059 (h) (1) e. 2 provides: "[A]ppropriate *costs* incurred arising out of activities and programs recommended by the advisory council that are not subject to contemporaneous recovery *shall be subject to deferred accounting treatment*...." In the world of utility rate making, "deferred accounting" means that costs incurred by regulated utilities that are subjected to deferred accounting are recoverable regardless of whether they are incurred during a base rate case test period. Where a utility is entitled to a return on its investment under deferred accounting, the return will begin to accrue when the costs are incurred. An example of why deferred accounting is required by the EE Amendments may be helpful. Without deferred accounting, if Delmarva Power were to incur $500,000 in a 12 month period developing EE programs, educating customers, and paying

5. Recovery of Costs and a Rate of Return: The EE Rate must include both recovery of the costs incurred by the regulated utility and a rate of return on the unamortized balance.[8] The phrase "return on the unamortized balance" means that a regulated utility is entitled to a reasonable rate of return on the portion of its energy efficiency investment that has not yet been recovered in rates.

6. Commission Approval Required: As stated above, the recovery mechanism recommended by the EEAC must be approved by the Commission before EE programs can be implemented.[9]

The recovery mechanism recommended by Delmarva in this memorandum is designed to comply with each of the mandatory recovery provisions set forth in the EE Amendments.

C. RATE COMPUTATION FOR DELMARVA POWER EE PROGRAMS

Delmarva Power's Maryland territory and Delmarva's affiliated utility, Pepco Maryland, have several years of experience with *Empower Maryland,* which is the name for the portfolio of energy efficiency programs that have been implemented in Delmarva's service territory in Maryland. The rate computation mechanism used for *Empower Maryland* utilizes a Commission-approved rate. The *Empower Maryland* mechanism does not place EE program costs in rate base; provides for annual adjustments; and has proven to be both efficient and timely. The rate computation mechanism proposed and described below for adoption in Delaware is based upon the mechanism used for *Empower Maryland* programs.

1. EE Rate Based upon Program Budget for Year-Ahead: The recommended first year of the EE Rate for regulated utilities will be established based upon the budget established by the regulated utility and the EEAC for the first year of the program. The EE program budget will include, *inter alia*, incentives to customers, equipment,

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contractors to implement EE programs for its customers, that $500,000 would only be recoverable if the 12 months during which the costs are incurred is a test year used in a base rate case proceeding. If the 12 month period during which that $500,000 is incurred in a non-test year for a base rate case, then Delmarva will not be able to recover those costs. With deferred accounting, however, Delmarva may defer the $500,000 regardless of whether it intends to use the 12 month period as a base rate case test year. The $500,000 in EE costs incurred will be amortized over five years and converted into an annual EE Rate without the need for a base rate case proceeding. Of course, because all amounts spent by Delmarva on EE programs will be recovered through the EE Rate that is adjusted annually, amounts spent on EE programs will not be recovered in base rates.

[8] 29 *Del.C.* § 8059 (h) (1) e. provides that regulated utilities are entitled to recovery of "appropriate *costs and associated rates of return* related to implementing activities and programs…."

[9] *See* footnotes 1 and 2.

installation costs, program and marketing costs, operating and maintenance costs, and costs incurred in the EEAC process.[10]

2. Amortization Period of Five Years: Delmarva Power recommends a general amortization period of five years for EE programs, which is the amortization period used and approved for *Empower Maryland* programs. There may be programs for which a shorter or longer amortization period is appropriate, depending upon various factors, such as anticipated life of equipment and customer rate impact.

3. EE Rate and Annual Amount Recovered – Year 1: The EE Rate is determined by calculating the annual amount to be recovered (as outlined below) and dividing that amount by the forecasted KWh load.

   The annual amount to be recovered would consist of the following components:

   a. Forecasted program costs;

   b. Forecasted amortization of program costs;[11] and

   c. Forecasted rate of return on the unamortized balance.

4. EE Rate and Annual Amount Recovered - Each Year Subsequent to Year 1: Subsequent to Year 1, the EE Rate will include the components outlined in Section C.3. above, to be annually adjusted as follows:

   a. Add forecasted amortized costs related to any additional EE programs recommended by the EEAC and approved by the Commission; and

   b. Adjust for prior period true-ups.[12]

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[10] In the event any revenues associated with the disposition of load savings become available, whether from within PJM-based markets or other sources, provisions to reduce the cost to customers by the amount of those revenues will be included in the EE Rate calculation.

[11] The forecasted amortization schedule is calculated by dividing the forecasted expenditures by the appropriate amortization period.

[12] Because rates are forecasted based upon Commission approved budgets, the actual amount recovered will be either above or below the forecast at the end of the actual rate year, requiring a true up the following rate year. On an annual basis, a true up will be made of actual EE Charge revenue billed in the previous year versus the revenue requirement for the period determined based on actual period sales, costs and amortization. Forecasted information is replaced with actual costs, amortization levels and required return on these costs using the Company's authorized rate of return. The recovery of these costs is included as part of the prior period true up. Fully amortized programs (i.e., after year 5) will be removed from the rate through the amortization true up process.

D. PROCEDURE FOR COMMISSION APPROVAL OF EEAC RECOMMENDED PROGRAMS AND A RATE RECOVERY MECHANISM

The EE Amendments provide that the EEAC shall recommend both EE programs and rate recovery mechanisms for regulated utilities.[13] The EEAC-recommended programs and recovery mechanisms must then be approved by the Commission.[14] This Section will address Delmarva's proposals for: 1. The Commission's procedure for approving EEAC recommended EE programs and a recovery mechanism; and 2. The Commission's procedure for approving annual EE Rate adjustments.

1. Recommended Commission Procedure for Approving EEAC-Recommended EE Programs and Recovery Mechanism

After the EEAC has made its recommendations to the Commission, regulated utilities will need to file for Commission approval of those recommendations. Because the Commission review and potential approval of a recovery mechanism will involve "rate making," evidentiary hearings will be required in compliance with the Administrative Procedures Act ("APA")[15] and the Rules of Practice and Procedure of the Public Service Commission ("Commission Rules").[16]

Delmarva will file an Application for Approval of the EEAC recommendations ("Application"). Delmarva anticipates that the Application will be supported by pre-filed testimony of at least three witnesses: (1) one Delmarva Power witness to testify concerning how Delmarva proposes to implement the EEAC recommended programs, (2) one Delmarva Power witness to testify concerning the EEAC recommended recovery mechanism (*i.e.,* how rates will be established and updated annually), and (3) potentially, one EEAC witness (*potentially the EEAC's technical consultant*) to testify concerning the EEAC's conclusions on matters such as: cost effectiveness, EM&V, and analyses performed by/on behalf of the EEAC. It is anticipated that a "traditional" schedule for the matter will be established, which will include: public notice, an intervention opportunity, public comment opportunity, discovery, the opportunity for other parties to submit pre-filed testimony, an evidentiary hearing, and briefing (if necessary).

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[13] *See* footnotes 1 and 2.

[14] *Id.*

[15] 26 *Del.C.* § 10124

[16] 26 *Del.Admin.C.* § 1001

2. Recommended Commission Procedure for Annual EE Rate Adjustments

The EE Amendments provide that the Commission must utilize a recovery process that provides for annual adjustments to the EE Rate.[17] The legislation further provides that the process used should be the same type used for "other supply resources."[18]

The only "other" electric resource that is currently considered by the Commission to be a "supply resource[]" is Standard Offer Service ("SOS").[19] SOS rates are adjusted annually to reflect: the results of the SOS auction for the year and true ups from the prior SOS year. The process used by the Commission for the annual SOS rate proceeding is not as formalized as the process used in a base rate case, nor is it generally adversarial in nature. The process is summarized as follows:

a. At least 60 days before new annual SOS rates are scheduled to go into effect, Delmarva files an annual application for approval of new SOS rates for the upcoming 12 month period.[20] The annual SOS application contains, among other things, rate calculations, spreadsheets and other information necessary to validate the proposed SOS rates.

b. At a regularly scheduled Commission meeting within a few weeks after the application is filed, the Commission issues an order that: (1) opens a docket for reviewing the annual SOS rate application; and (2) permits SOS rates, as filed, to go into effect subject to refund within 60 days.[21]

c. The proposed SOS rates go into effect 60 days after the filing, subject to refund.

d. Staff and DPA conduct an audit of the annual SOS filing. The audit includes meetings with employees of Delmarva's Compliance Pricing group, who

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[17] *See*, footnote 4.

[18] 29 *Del.C.* § 8059 (h) (1) e. provides: "...the Commission shall approve the recovery of appropriate costs incurred by Commission-regulated affected energy providers . . . in the *same manner as other supply resources*...."

[19] The SOS rate is the kWh rate charged for electricity supply for customers who do not chose to obtain their electricity supply from one of numerous Commission approved competitive retail electric suppliers. Although exact percentages vary by customer type, roughly 90% of Delmarva Power Residential customers are SOS supply customers.

[20] *See*, 26 *Del.C.* §§ 304 (a) and 306 (c).

[21] The phrase "subject to refund" means that a refund may be issued in the event that, after review, the Commission determines that the proposed rate that went into effect 60 days after filing was too high.

calculated the proposed SOS rates. During those meetings, Delmarva "walks" Staff and DPA through the rate calculations, responds to questions, and generally provides any information requested by Staff and DPA. Written discovery may be conducted as well. In the event that Staff or DPA discover any errors during the audit process, SOS rates will be adjusted for the remainder of the annual SOS rate period to account for the error.[22]

e. At the conclusion of the audit, Staff provides a report to the Commission that contains Staff's findings and a recommendation on Delmarva's SOS rate application.

f. Thereafter, at a regularly scheduled Commission meeting, the Commission hears testimony and issues its final ruling on Delmarva's annual SOS rate application. In the majority of cases, the Commission issues a final order making SOS rates final, "as filed."[23]

Delmarva Power recommends that the EEAC recommend an annual Commission procedure for establishing the annual EE Rate that mirrors the procedure used for the annual SOS rate proceeding. The recommended procedure would comply with the provisions of the EE Amendments, which require a procedure that provides for "efficient and timely recovery on an annual basis . . . *in the same manner as other supply resources....*"[24]

E. HOW THE EE CHARGE SHOULD APPEAR ON CUSTOMER BILLS

The EE Rate and total monthly EE charge should be identified as a separate line item on bills of regulated utilities, rather than being bundled as part of other rates. There are at least two primary justifications for this recommendation.

First, as addressed above, the EE Rate will be adjusted annually. The bundled distribution base rate, on the other hand, is only adjusted as a result of base rate cases, which take place, on average, several years apart. If the EE Rate is bundled with the distribution base rate (*meaning that it is not separately identified on the bill*), then when the EE Rate is adjusted annually, the bundled distribution base rate will also need to be changed. That situation would

[22] In the event an error is discovered that is so small that correcting it would have a de minimis effect upon SOS rates, Staff, DPA and Delmarva may agree to ask the Commission to allow the rates as filed to remain in effect for the annual period and wait until the subsequent annual SOS period to adjust the next year's rates to true up for the de minimis error from the prior year.

[23] As mentioned above, if an error was found during the audit process, rates are adjusted.

[24] 29 *Del.C.* § 8059 (h) (1) e.

be confusing to customers and would make it appear as though distribution base rates had changed, which would not be the case.

Second, failing to identify the EE Rate and monthly EE charge as a separate item on the bill would be inconsistent with recent action by the Commission to reasonably identify on Delmarva Power's bills the amounts that customers are paying for compliance with legislatively mandated programs. Pursuant to PSC Docket No. 13-250, (the "Billing Transparency Docket"), involving the Commission's review of the level of detail to be contained in Delmarva's monthly billing statements, specifically as it relates to legislatively mandated initiatives, the Commission adopted Order No. 8556 (April 29, 2014), which resulted in the following statutory programs being identified as independent line items on Delmarva bills: Green Energy Fund, Low Income Charge, and the Renewable Compliance Charge.[25] Delmarva Power supports the policy of identifying legislatively mandated charges on its bills that make bills easier to understand and more informative for its customers in general, without making bills confusing or unreasonably increasing costs of the billing process. Identifying the EE Rate and the total monthly EE charge on bills would be consistent with that Commission precedent.

[25] The Green Energy Fund line item represents the cost Delmarva Power incurs in complying with the statutory requirement to collect $0.000356 per kilowatt-hour from customers and forward these amounts to the State Energy Office to fund environmental incentive programs for conservation and energy efficiency in the State. The Low Income Charge line item represents the cost Delmarva Power incurs in complying with the statutory requirement to collect $0.000095 per kilowatt-hour from customers and forward these amounts to the Delaware Department of Health and Social Services to be used to fund low-income fuel assistance and weatherization programs within Delmarva's service territory. The Renewable Compliance Charge line item represents the cost Delmarva Power incurs in meeting the requirements of the Renewable Energy Portfolio Standards Act (or "REPSA"). This charge includes costs of solar renewable energy credits, general renewable energy credits, and the Delaware Qualified Fuel Cell program.